

PROCEEDINGS
OF THE SEVENTH ANNUAL
Institute on Accounting

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MAY 19 AND 20, 1944

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THE DEPARTMENT OF ACCOUNTING
COLLEGE OF COMMERCE AND ADMINISTRATION
THE OHIO STATE UNIVERSITY

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THE COLLEGE OF COMMERCE AND ADMINISTRATION

FOREWORD

The Department recognizes that the success of our annual institutes on accounting has been in part due to the persons who have appeared upon the program, and in part due to the persons who have so faithfully and regularly attended these meetings. Without a satisfactory attendance, it is impossible to secure outstanding speakers, and without outstanding speakers, it is impossible to attract attendance. We have been unusually fortunate in the last seven years in that the programs have been attractive and the attendance has exceeded expectations.

The attendance at the Seventh Annual Institute on Accounting exceeded that of any previous session. In view of the general conditions, this indicates that the subjects were timely and of interest to a large number of people. The subjects related to economic business and accounting problems of the war and the postwar period and were presented in every instance by well-qualified men.

The Department of Accounting is happy that they are able to contribute in a small way to discussions of this sort which may contribute to the better understanding and possibly the solution of some of the major issues. It is a pleasure for us to be able to meet our friends and renew acquaintanceships on these occasions. We hope that we will be able to continue these institutes regularly each year, and that you will continue to find something in these meetings of interest to you.

We hope this copy of the proceedings will remind you of a meeting well worth remembering. May we express our appreciation to you for your interest and support of these conferences.

THE DEPARTMENT OF ACCOUNTING
The Ohio State University

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FIRST SESSION

FRIDAY, MAY 19, 1944—10:30 A. M.

Commerce Auditorium

Chairman:

THOMAS J. DOLAN, C.P.A., *Wideman, Madden and Company, Toledo;*
President, The Ohio Society of Certified Public Accountants

Address: "Responsibilities and Training of the Postwar Accountant"

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Address: "Training of Accountants for Postwar Responsibilities"

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INTRODUCTORY REMARKS

By THOMAS J. DOLAN
Wideman, Madden and Company, Toledo, Ohio;
President, The Ohio Society of Certified Public Accountants

The Seventh Annual Institute on Accounting, sponsored by The College of Commerce, The Ohio State University, is now officially convened and, on behalf of the university, I take great pleasure in welcoming members of The Ohio Society of Certified Public Accountants, The National Association of Cost Accountants, members of the teaching profession, industrial accountants, and guests.

For a number of years The Ohio State University has very kindly and unselfishly sponsored these programs in the interest of the profession and in the interest of furthering accounting knowledge and study so that the programs benefit those of us engaged in public practice as well as those engaged in private practice and in the teaching profession. Like all previous meetings, I expect this one to be a grand success.

This Institute meeting was not planned primarily for the purpose of discussing the existing principles and practice of accounting, the ethics of the profession, current tax laws or 722 claims. It might best be called a preparatory session, planned and aimed at causing those of us who attend to think of the problems of the postwar accountant.

The postwar accountant will be confronted with problems of contract termination, the settlement of claims between the government and prime and subcontractors, the winding up of renegotiation, and the settlement of tax claims under Section 722 of the Code as well. Very likely there will be work to be done on the preparation and settlement of claims under the carry-back provisions of the Internal Revenue Code. Concurrently, he will be confronted with the accounting problems encountered in the conversion from a wartime to a peacetime economy and the cost problems of ascertaining, for competitive purposes, the cost of peacetime products. He must aid management to reduce wartime extravagances, inefficiency, and laxity, despite high labor costs which are going to remain with us, and he must, with these and the multitude of minor problems such as wage stabilization, price ceilings, controlled materials, labor contracts, and temporary unemployment, be a person of broad vision and be very much more practical than theoretical.

Such a situation means that the postwar accountant will not only require knowledge of the theory and practice of accounting; but, also, he must, I believe, broaden his educational background to include a knowledge of shop practice, engineering, economics, labor and personnel relations, and, last but not least, the law of contracts. As a result of the fine work of The American Institute of Accountants, in collaboration with The American Bar Association, our tax structure may be somewhat simplified so that more time may be spent in concentration on constructive business than in studying and trying to interpret complex tax statutes and regulations. However small the accomplishment of the Institute and the Bar Association in this direction, we must be grateful for the saving in time which will result, as time is most precious, particularly if we who are engaged in the accounting profession are to embrace even a slight knowledge of the fields I have mentioned. And yet, broad as the suggested range is, it is not sufficient. The postwar accountant must be more of an executive than he has been in the past. He must also have at least a speaking acquaintance with markets and marketing, with advertising, and also with research and development. Every war, while destructive in its purpose, does result in advancement in the field of science and scientific management, and, because of this, many nonprogressive individuals and corporations are going to be eliminated when the activity of war has ended. Some of those who suffer will have over-expanded beyond the ability of a peacetime economy to absorb their production. Others will have insufficient capital after excessive war taxes and renegotiation, and still others, who have both technical knowledge and capital, will suffer because of the inability of management to shrink operations and costs to a level of profitable competitive manufacturing and selling. Others will need improved facilities to replace those made obsolete and irreparable by use in this war program, but failure to have planned in advance will preclude delivery and installation of these few facilities in time to get under way. These considerations, whether they be considered management functions or not, are all the problems of the postwar accountant and we must consider them now.

I believe that the program planned for this Institute meeting, including the topics "Responsibility and Training of the Postwar Accountant," "The Nature of Postwar Accounting," and "Private Enterprise in a Planned Economy," as well as the talk on "Federal Income Taxation," will more clearly and in more detail enlighten us on these important topics. If the opinions expressed by your principal speakers are in conflict with the general thoughts expressed by me, at least such a divergence of opinion will cause those who attend to think of these complex problems and to use some

imagination in their thinking. If the Institute accomplishes no more than to make us presently conscious of the job ahead, it will be very much worth while.

Now may I present to you a man whom most, if not all, of you know either personally or by reputation, a man whose works in the accounting field are recognized as authoritative and are a "must" in every accounting library, a man who has spent so much time in research, teaching, and writing that his opinions are most valuable. I am, and I know you are, most anxious to hear Professor William A. Paton, Certified Public Accountant, Professor of Accounting at the University of Michigan, and author of reference and textbooks on accounting, as well as many articles of current interest. Professor Paton.

RESPONSIBILITIES AND TRAINING OF THE POSTWAR ACCOUNTANT

By WILLIAM A. PATON, C.P.A.

Professor of Accounting, University of Michigan, Ann Arbor, Michigan

The chairman has already given an excellent outline of the responsibilities of the postwar accountant, a very definite and concrete list of comments. I am glad he has been definite and concrete because that will give me still more of an excuse to be vague and indefinite in my remarks.

As I understand it, this topic was assigned to Dean Scovill and myself with the thought that, insofar as practicable, I would concentrate upon the "responsibilities" and he would tell you about the "training." Both phases of the subject are of course closely related.

This is a speculative and difficult topic to deal with, except in rather general terms. To begin with I would like to talk about the general environment of the postwar period, because it seems to me that the work which the accountant will have to do in this period depends very much upon what the environment is going to be.

I would like to discuss the subject primarily from the standpoint of the professional accountant. In emphasizing that side I do not mean to restrict our conception of postwar accounting to the public accountant's area; accounting is a broad field, and there are of course many people in accounting whose work does not fall strictly within the realm of professional accounting in the usual sense. I think, however, that it will not be inappropriate if we have the public accountant's task particularly in mind, because the work in other sectors of accounting will be related, to some extent, to the work of the public accountant.

I want to speak first of what I consider to be the outstanding question regarding our postwar environment. It is the question of whether we are going to have some sort of state socialism or some form of private enterprise. I do not mind saying right at the outset that I am not a state socialist. Far from it. In fact, thoroughgoing collectivists are not very common among accountants. Any poll I have been able to take has always shown that the majority of the accountants are hoping that the environment of the years ahead will be such as to permit private enterprise to function effectively.

I do wish to imply that there is necessarily anything sinister to an

accountant about state socialism. I can sit down and talk in a perfectly friendly way with a person who is anxious to see government control intensified and spread over practically our entire economic life. But there is one aspect of our present situation that does annoy me; I don't like the persistent efforts of a lot of folks in high places to establish a state socialistic program while at the same time giving lip service to private enterprise and the maintenance of our system of private enterprise. I have no complaint to make with respect to any person in our society who has taken an honest stand for collectivism or state socialism, but I do not like the crew who, while making some pretense of favoring a continuation of private business, are nevertheless busily engaged in an effort to scuttle private business by destroying the conditions and factors necessary to the successful functioning of the system.

Now the question is, what effect upon accounting—accounting principles and accounting practices—can we expect if something in the nature of a thoroughgoing state socialistic program is developed in this country in the next few years?

Years ago I often took this question up in my classes as a purely theoretical question. We enjoyed spending a half hour or so speculating on what effect state socialism would have on accounting theory and accounting practice. I thought of it then as an academic question. It seems to me that it has become thoroughly practical at the present time. We have taken a long, long stride in the direction of government management and operation of industry.

There are two major functions of accounting, as I see it, and they are closely related. In the first place, we are interested in the management of business. We are attempting to facilitate effective management, effective administration of economic conduct, particularly in the organized business area. In the second place, we are interested in promoting equity between the parties at interest in this area of business activity, private business activity. Now those two considerations would still be with us, of course, under any collectivist program. Whatever system of government we have, whatever system of carrying on economic activity we employ, presumably it will be desirable to run it well and to run it with an eye out for equitable treatment of interested parties. My own hunch is that both of these angles of business operation tend to be somewhat obscured under full-fledged government control, but that, undoubtedly, is a moot point, since it is just as important that business be run well and be run equitably if the government is running it as it is desirable to have those criteria observed when somebody else is running it.

Against this general background, it is possible, as I see it, to make two or three fairly definite observations. Income accounting, as it has been developed, would probably be minimized somewhat under a thoroughgoing socialistic regime. In governmental accounting at the present time the stress is not upon the measure of profits, the matching of revenue and costs. And even where government undertakes what we think of as an ordinary commercial activity, the absence of private equity capital tends to eliminate or modify sharply the process of determining profits or any form of "net" income balance.

If that observation is sound, it follows that it would take some of the interest out of accounting—for me, at any rate—to have business run as soviet or sections of some general political or governmental control. I think that many of our most interesting questions in accounting, many of the things we have the most fun with, many of our most controversial problems, have to do with the process of measuring and assigning periodic income for particular business institutions, and any move in the direction of minimizing attention to that process would perhaps take a little of the spice out of life as far as accounting is concerned; certainly it would change our direction and emphasis.

Now, turning to cost accounting, it seems to me that cost accounting tends to be emphasized more roundly under a highly controlled situation. That is, as you minimize the possibilities of controlling business through private enterprisers' attention to a more or less freely-moving price system, you naturally tend to shift to cost compilation as a means of deciding what to do, and deciding what the rights are in a particular situation. I would expect, therefore, that as far as cost compilation and cost measuring, and the other general problems of cost accounting are concerned, they would be magnified somewhat in the postwar period if we are going into state socialism. I am not saying we are going state socialistic. I will make a prediction shortly, but I think that there is enough of that trend in the air to cause us to contemplate what the influence of such a change would be on the development of accounting.

As far as the clerical—red tape—side of accounting is concerned, there will be more of it. I think it is evident that whenever politicians or government officials of any kind take over an activity, they do not tend to cut down red tape, as has been sometimes done under other methods of management, but to magnify it. I picked up something on the train as I was coming down. It hasn't much to do with accounting but it illustrates this point. It is an article put out by the Automatic Control Company, and it emphasizes this aspect of red tape in the use of language. It says: "The

creation of the world is told in Genesis in 400 words. The Ten Commandments are propounded in but 297 words. The immortal Gettysburg address contains 266 words. The Office of Price Administration uses 2,500 words to announce a reduction in the price of cabbage seed."

I think that under complete governmental administration of business we would have a great stress on what you might call the stewardship aspect of accounting, the discharging of responsibilities in the relatively narrow sense. Take a government storekeeper, for example. He would be keeping track for dear life of every unit of stuff that came under his influence and he would acquit himself of responsibility when the stuff left his hands; he wouldn't care greatly how much went out or where it went. It may be smashed later, but he is going to have a record showing that it went through his hands. I suspect that record-keeping procedure would tend to be glorified beyond anything we have known yet under complete government operation.

Now as to a prediction about the future, a prediction as to what we are really going to be facing in the next couple of decades. Are we going socialistic? Most of you would say right away that the answer is no, and I am inclined to agree. I am inclined to make that prediction, but I am not sure but that my prediction is based on wishful thinking. I do not want the government to run everything, so I have a tendency to predict that they are not going to do so in the future. Once in a while I begin to wonder. I think it depends somewhat on how long this war lasts. We certainly have a very pronounced government control of everything at the present time. When you can't fire a man and you can't hire a man and you can't do the ordinary things that we associate with private business management, it means somebody else is boss. You could do away with all the rights of private management without taking the stock certificates literally away. We could still keep those fancy pieces of paper, notable examples of the art of printing. We could even ride by the factory and say, "That is my factory; I have so many shares of stock." But if I haven't any control over it, or any economic rights in the situation, then, of course, my ownership, my influence, has become just a shadow. You do not have to have formal repudiation of private property in one fell swoop in order to have what I would call a state system of business operation. In Germany they have stock certificates still; they have all their former rights on paper, but the government is the boss.

Now, I sometimes think that there is really a serious danger, if you want to call it a danger, a serious possibility, at any rate, that we will go into the postwar period strong for that sort of thing instead of having a

reversion in the other direction. However, I am going to predict that although the trend for a good many years has been toward more and more government control of business activity, more and more immediate government influence in business activity—that trend has been very persistent and it started even before the Roosevelt era—it is not going on indefinitely. If you look over history carefully, you will find quite a bit of evidence of the zig-zag, of ebb and flow. Now we have been on the zag for quite a while and I want to get back on the zig, and my prediction is that there is a fair chance that I may see a little of the zig again before I die. In other words, this very persistent, very pronounced trend to take away our rights to run our own affairs, one by one, may be reversed.

My conclusion or prediction is this: we are not quite ready in this country for anything as complete by way of government control as they have in Germany or as they have in Russia, and are not likely to be ready for it for quite a long time. The Montgomery-Ward incident tends to show our basic attitude; there was a genuine resentment among many people who are ordinarily supporters of our government over that episode. It did not mean they were great pals of Sewell Avery, but the action of the government in sending soldiers in to carry him out of the office, over some technicality that the courts ought to be able to settle, struck a lot of people as rather extreme. That picture in the papers looked a great deal like a lot of pictures that could have been taken in Germany in the early days of the Nazis. They did not take people into concentration camps in the early days, right off the bat; they just elbowed them around. A little more than ten years ago most of the Germans wouldn't have had the faintest idea that Hitler was going to be able to get the range of power he did finally. The reaction to this little Montgomery-Ward episode showed quite clearly that this country has too many divergent points of view, is too big a country in geographical area, and so on, to fall into a complete socialistic pattern readily in the next few years. I think we are going to have a very interesting time. I think what we are going to do is remain right in the middle of this question for a decade or so, with some backing and filling, without any complete clear evidence as to who is going to be boss in business.

The government, without doubt, is going to have a finger in the pie to a great degree in the next few years. That is obvious. That is inevitable in view of some of the problems our chairman called attention to, in view of some of the definite problems facing us as a result of war conditions. It is going to be a complex situation and it is going to be a tough spot to be in, in many ways. It is quite a chore to tie the business mule so tightly that he

can't kick and at the same time leave him enough leg room so that he can do the plowing.

If we do remain somewhat in the middle of the stream with respect to who is boss in private business and who the accountant is going to work for, this will certainly have a bearing on the accountant's responsibilities and on the concrete nature of his job. If he is working for private business, that is one thing; if he is working for government, that is another thing; if he is out in the middle because the whole problem is out in the middle, that is still another thing.

Let us assume, as one possibility, that the next twenty years is going to see the liquidation of what is left of the rights of private business. We are going to need lots of accounting in that liquidation. I would say that the accountant is going to be right up to his ears in responsibilities of somewhat the same nature he has had—intensified along certain lines—if we assume we are going to liquidate the private enterprise system through a gradual establishment of more complete government control. The accountant will be assisting, don't you see, in the liquidation. It will be like the termination of war contracts, only running on for a couple of decades, trying to get the question settled as to who is running the thing, and I am going to assume the accountant will be a right-hand man in that event in carrying forward the liquidation.

Suppose we go the other way, and we decide to rehabilitate private enterprise. Private enterprise does need some rehabilitation if it is going to run things. I have been noting a very interesting experience in respect to our student body for a number of years. Back twenty years ago frequently a young man would drop into the office and ask for fatherly advice that a professor loves to have the opportunity to dish out: He was thinking of going into a little business of his own; and he had about \$1,000 and his prospective father-in-law was going to put up \$5,000 more and they were going to develop a patented device for jumping out the window in the case of a fire without breaking your neck. People dropped in often twenty years ago and talked to me about such plans. But it is literally true that I haven't had one single instance of a young man graduate of the University of Michigan coming in to talk of anything of that sort for the last ten years, not one single instance! I have sometimes raised the question, and I have found they were immediately horrified—"I wouldn't tackle anything like that! It is too risky. Heads I lose and tails the other fellow wins. There is no motive. If I should go into business and make some money, I would lose it all in taxes anyhow."

I maintain seriously that, in order to have private business function

and go on and do the experimental work and develop new products and all that, there must be some inducement besides just saying to a fellow, "Get out there and hustle." There must be an economic inducement. Without such inducement the prospective enterpriser would rather be an employee of the government or of some already established business. It is going to be interesting to see, in the next five or ten years, whether something is done to give the small, new business concern a chance, and, if something is done, it is going to have accounting repercussions.

Suppose we say that in the small business, the new business, you can deduct the cost of your capital in any way you please in your tax return. You have to invest \$100,000 in machinery. You can charge it all to expense in the first year if that suits you from the standpoint of your income tax return. There is an interesting possibility. I believe I would recommend just that sort of procedure on the part of the Treasury, perhaps not quite so extreme as that, but I would go pretty nearly that far. Let these fellows amortize their investment in any way. This suggestion, of course, is more or less in violation of the concept of accrual accounting we have built up through the years; it raises the distinction between a sound financial relationship between a young business and government and the ordinary process of matching revenues and expenses.

There are a lot of interesting things that one could touch upon as to the possibilities of stimulating small business enterprise. I am very much interested in that question, and I think that, while a lot of lip service is being given to it, it is not obvious that anything concrete is going to be done that will be genuinely helpful. I suggest that you watch developments in the next five years and see whether or not an environment is created which enables people to take chances, take risks, along the business line.

But whether private enterprise is liquidated or rehabilitated, for the next twenty years, we are certainly going to have a tremendous lot of accounting, and I do not see any substantial reason for expecting that the responsibilities of the accountant will be minimized, or the interesting parts of his work eliminated, during that period.

There is another question in addition to this government control aspect, somewhat related thereto, that I would like to mention. I have been wondering quite a bit in the last few years about what is going to happen to the corporate institution. As you all realize, we have a system of taxation which is very unfavorable to corporate enterprise. In fact, there have been quite a number of instances of small corporations unincorporating and reverting to partnerships or sole-proprietary forms of activity, and one of the reasons for this certainly has been the unfavorable tax set-up which exists

as far as the corporation is concerned. It is interesting to speculate on what may happen to corporate accounting if there is some further tinkering with the corporate entity. You could put it this way, what is going to be the significant accounting entity of the future?

Of course, if we have state socialism or something of that kind, maybe a municipal organization of some kind would be the significant accounting entity. As a matter of fact, the question of entity has always been unsettled. I think the accountant has sometimes been somewhat confused as to what is the basic, significant entity. Somebody ought to sit down sometime and work out a little book or article on that particular question. For instance, you have the department concept in accounting, the legal-company concept, and the group-of-legal-companies concept.

You all know of cases in which department managers have resented the orthodox accounting system which did not permit showing a profit for the department, particularly if it was a service department or an integrated department back three or four steps from the line of sales. That has been a sore point, managerially speaking, for a long time. Take companies, for instance, in foreign trade. When they produce on this side of the water and sell to a branch on the other side, the sales are all over there. At one time the League of Nations organized a committee, and one of our accountants in this country worked on the report, to try to work out some scheme of allocating the effective results to those two departments. Of course, they were particularly interested in taxes from the standpoint of the different governmental jurisdictions that were associated with the tax problem in the case of the business that crosses the geographical lines of a sovereign state. That is a very unsettled question. I do not think that the accountant who emphasizes the legal company as the basic entity can always do a fully satisfactory job from the standpoint of showing departmental interests what the picture is. But as long as taxes run in terms of the legal company, and a lot of other charges run in terms of the legal company, it is going to be very difficult to compute an income statement that means anything for the smelter, for example, which delivers its product to a refinery or some other outfit a step along the line that is in the same corporate area, and makes no sales in the ordinary sense.

Management sometimes thinks we ought to have some accounting for the department. The law generally sets up the legal company in the corporate field. There are folks who think that the consolidated statement for affiliated companies is really the significant thing. For instance, our friends in the Federal Power Commission are busily engaged running up and down the country, mainly interested in this question: How much is

there in the property account of the public utilities which represents profit to affiliated companies from whom these assets were acquired? Their theory is that if Company A has even a nodding acquaintance with Company B, Company A is not justified in transferring goods to Company B at any figure except cost. They seem to have more confidence in cost accountants than I do. I would say it would be a horrible system from a management standpoint, from an equitable standpoint, from the standpoint of the effective utilization of resources, actually to enforce a requirement that if you know the buyer, the product must be transferred at cost, even if he is only a sixteenth cousin. They have actually carried that idea out in cases where only one-eighth of the stock was intercompany. They have insisted that the property account must show cost to the affiliate, and not fair market value at the time the property was transferred to the other entity. That is the consolidated point of view, with a vengeance.

I would just like to suggest in this connection that I think that is a very dangerous point of view to emphasize in accounting. My concept of the consolidated statement has always been this: It is a supplement to and not a substitute for the statement or statements of the respective legal companies in the group. I have always liked the practice of the American Telephone and Telegraph Company, which publishes the actual legal-entity balance sheet of the American Telephone and Telegraph Company along with the consolidated statement of the Bell System. Of course, if there is just one little subsidiary folded into the big company in a consolidated statement, it doesn't make enough difference to matter, but I do not like the idea of consolidating two or more important companies and issuing only one set of statements, even though we do have consolidated tax returns under certain conditions. We haven't always had such returns. There has certainly been a zig-zag there, as there has been in many other tax matters. The creditor of a particular company cannot depend upon consolidated assets. All he can depend upon is the assets of the particular corporation that owes him money. The preferred stockholder in the particular corporation must depend upon the assets and earning power of the particular, specific company. The minority interest, if any, must depend on it. The employees must depend for their bread and butter on the affairs of a particular company. In other words, unless the legal structure is changed much more than anything we see on the horizon now, I would say that for the future, as in the past, the point of focus in our financial reports should be the specific corporation created by a certain jurisdiction as the significant accounting entity in the corporate field, rather than that company plus three or four or more other companies, all wadded in together, with which it happens to be related.

I regret to say that I think there have been a few public accountants who have said things and done things that have tended to lend some support to the view that it is the consolidated statement that is the really decisive statement in the case of a group of affiliated companies. I would like to have you ponder that point. There is no time to discuss it in detail, technically. I think it is an interesting technical question, but there are some people at the present moment who are veering in the direction of saying that the consolidated statement is really the significant thing. That has some interesting repercussions, if you carry it through. It tends to deny the reality of a profit or loss even though the transfer is on a thoroughgoing market basis, providing the parties are affiliated. I do not believe we would ever succeed in dividing up all the businesses in this country into water-tight compartments representing the affiliates on the one hand and the non-affiliates on the other. There is a gradual gradation from those which deal at almost complete arm's length, to those who have a slight nodding acquaintance, to those who are considerably affiliated. I won't deny that the affiliation might be so complete in rare instances that the significance of the statements of the individual companies might be slight. There may be such instances, but let's not set that up as a standard.

While our chairman has referred to it, there is one other thing I want to mention about the corporation situation before we leave the subject. There is another tendency or condition in respect to corporate affairs of special interest to the accountant. We are urging more or less continuously as to whether the corporation is an association of individuals or whether it is a separate and distinct entity in itself, and court decisions and administrative decisions indicate a pawing over of that question. That is going to be an interesting point for the future to settle. It has quite a few accounting angles. If, for instance, we accept the association or partnership concept of the corporation, then the minute that the corporation earns a dollar, it perforce becomes income to the partner-stockholder. Now that will have some very interesting ramifications taxwise if it actually becomes the dominant theory. Looking at the corporation books, if that became the dominant theory, it would practically do away with surplus accounting (and maybe that would be a blessed good thing), because you would be in a position just as in partnership accounting to credit each stockholder definitely with his distributive share of the earnings the moment they were determined, and such distributive share would be in effect a current account, practically a liability. There are other interesting ramifications. That question is not settled and it is going to be under dispute in the coming years. My impression is that there is more sentiment in various influential circles for the

association point of view than has been true in the past, and that general problem must be solved, or molded in certain directions at any rate, in the years ahead of us. And the way in which it is settled or liquidated or developed will have quite a bit to do with some very controversial accounting questions and thus will have something to do with the environment and task of the accountant.

Mr. Dolan was telling us about some of the things that the accountant is going to have to do in the immediate future. I am inclined to agree with the flavor of his remarks in that connection. Of course, we have a considerable job on our hands in dealing with the complications that are involved in this tremendous relationship between business and government. We used to think that the government was the best possible customer. Perhaps we still should. But I do not think that there has ever been a time since I have been interested in accounting, which is a matter of over 30 years, in which financial statements were so hard to deal with and so uncertain in their implications and meanings as at the present time; and this, largely, grows out of the times and the fact that the government is the principal customer. Straightening out government accounts is no sinecure. There are obvious reasons for that. Whether the Controller General has his way or not, there is going to be quite a lot of fussing with these transactions for some time to come. If Congress can't find anything better to do, think of the investigations they can start after the war is over to keep them busy during the postwar period in regard to the transactions in the war period. Accountants are going to be very active in this area of settlements with government for some time to come.

Let's take a look at the tax situation, particularly tax simplification. I think that it would be a fine thing if our tax work could be reduced. It would be a wonderful thing if we would quit fiddling with the tax structure and passing retroactive legislation and settle down to a clear-cut system which varied only in rates. There is bound to be a variation in rates as the needs change.

According to the recent news releases, there are some prospects of simplification in the corporation tax structure. That is the thing accountants are especially interested in, and that, by the way, is the phase of tax accounting that, it seems to me, has been most seriously in need of reform. All this talk about simplification of the individual return and making it possible for 30 or 40 million people not to file returns, I am frankly not very much sold on. I do not mean that I don't want to see simplification there, but there are two sides to that story, and you may have too rough a situation, too much inequity, if you go too far in that direction. It is a healthy thing

to require a citizen to sit down, figure his tax, and file his return. It is conducive to restraint in government spending. It would have been better if we had had 30 or 40 million filing right along instead of the few million we have had.

But the corporation tax has become almost fantastic in its elaboration. A person tends to think he is reading Alice in Wonderland when he starts studying it. It is badly in need of attention. I would be glad to see the complete elimination of the corporation tax as far as the tax on income is concerned and the shifting of the tax entirely to stockholders as individuals, but I realize that is a big question. At any rate, there are possibilities that the accountant's task in connection with the corporation tax will be minimized through radical simplification of this form of tax.

I would like to say a word about the auditing situation, and stick my neck out just a little bit here. Auditing work has always left me rather cold. I am not an enthusiast for making checkmarks, and I can't talk with a great deal of enthusiasm to a bright young man who is wavering between law or going into accounting about checkmarks and all the other menial tasks that are associated with a good deal of public accounting.

I do not disdain humble tasks. I tried to build a bird house a while ago and I discovered there was a lot to even such a job, that there are about 100 things you can do wrong at practically every stage of the operation. Even the humble chores in this world are worth doing, and there is a great difference between doing them well and hashing them.

But we are face to face, as you all know, here in wartime with a situation in which it is almost impossible to grind out the amount of verification or routine checking which we have done in some instances in the past, and I hope we can capitalize on that experience and get out from under a lot of it in the future. That may sound as if I am talking against the interest of the public accountant. But I am speaking only of auditing in the sense of detailed checking and verification. If we are to have a great mass of auditing of this character, I suggest that we consider it a separate business and not call it professional accounting. Let's sort that out. There are large staffs of clerks employed by business organizations who do that type of work. Let's have public accounting operate on a little different plane. I recognize, of course, the need for sound detailed procedure and accurate computation in connection with all phases of accounting work. I am simply throwing out the hint that perhaps the amount of this sort of work may be somewhat reduced in the field of public accounting and greater emphasis placed on analysis and technical advice.

That raises the question, of course, of what will be the future of these

big firms. It can be argued that these large firms are more like business enterprises than professional organizations. One reason, of course, for the growth of the very large firms has been the volume of detail work that has been associated with public accounting.

Just as a suggestion, then, I am going to express the hope that routine auditing is going to be minimized somewhat in the years ahead or will be segregated as a separate type of activity. It is associated with the professional aspects of accounting, but, in itself, is not highly professional. We would all, of course, like to see accounting develop in the future particularly along the line of its professional aspects, growing to full stature among the outstanding professions. As pointed out by our chairman, the accountant of the future must be a person who is uniquely prepared to grapple with the problems of a financial and managerial character in organized business, with a view to directing the processes of business or assisting in directing the processes of business more effectively and assisting in settling the rights of various parties, including government, in the business situation.

Each one of us tends to glorify his own line of work, but it does seem to me, seriously, that the accountant has a marvelous opportunity to step into a niche that we see somewhat vaguely now, which involves economic analysis, financial administration and managerial techniques, along with general accounting. There is certainly the possibility that accounting may come to be rated as the top profession in the business area. However, if we are to achieve such a status, we must attract high-grade people to the field, and we must emphasize the truly professional aspects of our work.

I don't think the term "accountant" fully describes what I have in mind, yet it is not a bad label: Accounting is a double-jointed process of measuring business forces, and of arraying those measurements and translating the arrayed measurements into effective action. I don't believe there is anybody better suited to the task than the accountant. We have made a start in doing that job; and, in order to do it thoroughly, we must have the whole grist of qualifications that Ed Wilcox was telling us about in a meeting in Chicago last fall (I think his paper appeared later on in the *Accounting Review*). He certainly set up a bill of particulars of an impressive sort in describing the kind of a man, the qualities that are needed for public accounting. I believe he was thinking ahead and taking a good look at the difficulties that lie in front of us.

The accountant has to be a financier-manager-economist-accountant to step into the top-flight position in the postwar period, and it seems to me there is waiting for him a place which will be top-flight, whether we liquidate private enterprise or whether we rehabilitate it.

CHAIRMAN DOLAN: Thank you, Professor. As usual, you have covered a lot of territory in a very short space of time. I can certainly say you are not alone with the OPA in the illustration you gave earlier in your talk.

You startled me at the outset in talking about state socialization and government control, but your prediction finally straightened that out. I am glad we can pretty generally agree with you. I have great confidence in the American public as a whole, and I don't think 130 million people will be misled forever.

The responsibilities of the postwar accountant have been covered very thoroughly by Professor Paton, and now we know what those responsibilities are. We will have to know how to prepare and train to assume and take care of those responsibilities. Our second speaker this morning, Dean Scovill, Professor of Accounting, College of Commerce, The University of Illinois, is also a past president of the American Accounting Association. He is past president of the Illinois Society of Certified Public Accountants and has been a member of the teaching profession for a number of years. He is editor of the Wiley Accounting Series, and, like Professor Paton, is the author of a number of books and a number of interesting papers. I think we can round out our morning session by hearing Professor Scovill on "The Training Required for Postwar Accounting." Dean Scovill.

DEAN H. T. SCOVILL: Mr. Chairman, Friends of the Institute: I have been very much interested in Professor Paton's dissertation on the responsibilities of the accountant, because if I have to match up the trends in the positions with the responsibilities, it is interesting to know what the trends might be.

In general, I agree with Professor Paton on many points. I am not sure I would want to go all the way with him on the matter of home corporation and consolidated statements. I am not sure I would want to go all the way on the matter of checking on the part of junior accountants. I still think there is a great opportunity for the junior accountant to learn many things in accounting, and if he keeps his mind on his work and checks intelligently, then I think it is not much worse for a junior to spend a little time now and then checking and learning about the procedure than it is for a young lawyer to spend a great deal of time running from one court to another to file a document here and a document there and looking up indices and doing other menial tasks. However, I won't argue that too long.

As I look at this topic and see where we are trying to go, where we think we are going, I am reminded of a story of the young boy that was in a small town at the railroad station. He saw on the baggage truck a box or a crate in which there was a pair of rabbits. He got playing around with the rabbits and finally stuck his hand through the crate. Finally, the crate opened and a rabbit ran out. The boy realized what he had done, so he ran after the rabbit, chasing him to the edge of town. Finally the rabbit ran through a hedge and the boy said, "Go, darn it. You don't know where you are going anyway. Your tag is back there on the box."

I wonder if we know where we are going. If our tag is somewhere, I hope it is the type of tag that was made out prior to 1933, because some of the things that have happened since then are not some of the things we would like to see proceed indefinitely.

TRAINING OF ACCOUNTANTS FOR POSTWAR RESPONSIBILITIES

By H. T. SCOVILL, C.P.A.

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It is assumed that we are not expected, at this time, to discuss questions which affect primarily educational institutions in dealing with their problems in the immediate postwar era. Such problems constitute separate subjects and require treatment distinct from that which should be accorded this subject as we interpret it. Universities have their own postwar problems of offering special concessions in courses, methods of presentation, acceleration, and refresher material for those who return from war positions, either civil or military.

The subject to which we shall address ourselves today deals with the training of accountants for the types of positions and duties they will be expected to perform in a peacetime economy. Such training may be in college or elsewhere. It may be for professional accountancy or for positions in private business concerns.

There is an implication in the subject that training of accountants for postwar responsibilities is to differ materially from that offered for prewar responsibilities. If training is to be different it must be for one of two reasons: (1) that postwar responsibilities are to be so different in nature that they will require a different type of training; or (2) that the training before the war was inadequate even for the purposes then existent.

Professor Paton and I are in substantial agreement as to the nature of postwar responsibilities of the accountant. Unless governmental regulations are modified considerably, the postwar public accountant will continue to make audits and examinations in accordance with about the same type of procedures as in the past, but the form, extent and nature of the statements, disclosures, reports and analyses he prepares therefrom will be subject to control of other agencies even more than in the last ten years. In other words, the public accountant will probably continue to be somewhat affected by the whims of a new quasi master as he has during the last several years.

One important objective in the training of the future, therefore, will be to impress upon the prospective public accountant the importance of establishing sound and consistent principles, policies, and procedures so that

they will stand the test of subsequent scrutiny and criticism, even by those who might not be in full sympathy with the doctrine of free enterprise.

Just as there have been different schools of thought in the past on the best type of training for accountants, so there doubtless will be in the future. It is generally recognized, however, that an accountant should be able to use figures rather readily and to make at least simple types of arithmetical and mathematical computations even if his ultimate duties as a public accountant might be of a consulting character. It can generally be assumed, I believe, that unless one has been reasonably successful in secondary school with those subjects requiring accuracy in thought, if not in calculation, one will not be very likely to try to adopt accountancy as a career.

The differences of opinion in the past on the type of formal university training for an accountant have rested principally on the relative amounts of technical and general subjects. There does not seem to have been agreement, however, on what is technical and what is general. A study of the programs of 127 recent (prewar period) graduates from the University of Illinois reveals the following typical distribution of subjects:

	<i>Semester Hours</i>
Mathematics and other sciences	13
Foreign language	8
Rhetoric and speech	8
Literature	8
	<hr/>
	37
History, government, sociology, philosophy	15
Social economics	17
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	32
Business economics	9
Business administration, law, marketing, etc.	15
Accountancy	32
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	56
	<hr/>
Total hours, exclusive of physical education, hygiene and military	125
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It appears, therefore, that 55 per cent of the 125 hours of so-called academic subjects was of the general type and 45 per cent, of the professional type. This classification ignores, of course, the value of some accountancy courses as a substitute for mathematical reasoning, and of the business

economics and business administration courses as substitutes of an applied economic character for the social economics courses.

This division of subjects is typical, we believe, of most middle western universities that pretend to train young people for positions in professional accountancy or as accountants in private business. Such a curriculum provides a reasonable division between the technical and the general.

The use of machines, especially the punched card type, in the book-keeping and accounting departments of business has been increasing for several years and will doubtless continue to be popular in the postwar era. It would seem that accountants trained in the future should be exposed to such machines sufficiently to appreciate their general usefulness, adaptability, limitations, and effect on auditing procedure.

Educators in accounting will probably feel that some changes will be desirable in the formal training of accountants for postwar responsibilities. It would seem strange if no changes were proposed, because the demands on the accountant are changing to some extent, and those in charge of training methods should at least try to keep pace with demands. Medicine and law are old professions compared with accountancy, yet the educators in those fields are making changes from time to time.

Greek and Latin were at one time thought to be essential to a good legal education. Now other subjects have crowded them out in many pre-legal curricula. Similar shifts in emphasis might be cited in other fields as engineering, architecture, chemistry, and even in the ministry. The mere fact that an educational plan for a given profession or calling is likely to require changing from time to time, however, should not deter one from suggesting a reasonable, workable plan; or from describing some plans that are yielding good results at the present time.

We have heard professors of law advise students that any course in the University might be unusually beneficial at some time or other in their careers as trial lawyers in interpreting or understanding evidence or in preparing a case for a client to be treated either in court or out of court. There is much truth in the statement. We could doubtless claim similar truth for a statement of like character made to students who expect to become professional accountants.

A knowledge of botany, zoology, chemistry, physics, bacteriology, or other science might prove valuable in auditing engagements from time to time. Although principles of economics is a subject all accountants should study, there are a number of other phases of economics which might prove helpful from time to time even though a single individual would probably not be able to study all of them during his university career, in addition to

other subjects which seem desirable and necessary. Some of these are foreign trade, tariff, labor policies, insurance, economics of public utilities, principles of transportation, theory of money, and, of course, private and public finance.

As I see it, the professor of accountancy does not have nearly as hard a time in selecting a given number of credit hours of each of several fields of knowledge to be pursued by the student in his field as he does in convincing the student that the curriculum outlined is a reasonable one to follow for his purpose. The curriculum available to the student is usually flexible, permitting a number of free electives to be chosen within reasonable bounds by the student. But the professor is regularly confronted with the necessity of emphasizing the importance of a fairly broad education as evidenced by the curriculum, and of directing educational interests along channels other than those measured by specific courses. Some of the things that should be given consideration, for example, are discussed below.

Overspecialization—It is generally pointed out that in order to become a good professional accountant one must study many subjects other than accountancy. At Illinois we do not permit a student to take a second year accountancy course until he has reached second-year status in other subjects. He cannot begin his third year accountancy course until he is a full-fledged junior and so on. Thus, he is required to pass rhetoric, mathematics, other sciences, principles of economics, language, literature, history, political science, philosophy, and other subjects before completing his third year course in accountancy. Accountancy courses constitute slightly less than one-fourth of the total hours required for graduation.

The question of breadth of study in a given area of knowledge occasionally arises. For example, if 15 credit hours of social sciences, other than economics, are required, should one suggest that the student take the elementary course in each of five fields or take all 15 hours in history, all in philosophy, or all in some other field? In general, it seems best to have one's courses of this type spread over a wide area so that one's interests will be broadened. If one is exposed to the fundamentals in each of a number of fields one is more likely to have broader interests in life and to pursue additional reading in those fields of one's own volition. In other words, he will feel that he has a speaking acquaintance with many fields, any one of which he can explore further when and as appropriate. As the little girl said in her essay on parents: "We get our parents at an age when they are so old it is difficult to change their habits." If universities do not attempt to create proper habits of reading widely while dealing with individuals at school age, such individuals will probably soon be too old to change their habits.

Lack of Perspective—It is often necessary to remind students that they are spending a few years now getting ready for the next 50 years of active and presumably useful service. They should take advantage of all opportunities, and not shun the courses which are considered to have educational value just because they do not seem to be in their chosen fields.

Tendency to Take Only the Minimum—A definite number of credit hours is set as a minimum for graduation. From the frequency with which this minimum is also regarded as the maximum one would think a penalty existed for exceeding such minima. Very few students can be induced to take more than the required number of hours even though there are scores of valuable courses available which more mature people can visualize as ultimately valuable in one's sphere of activity in later life.

Memorization and Thinking—We in accountancy educational circles try to emphasize the importance of thinking things through to a logical conclusion—of starting with fundamentals and building the super-structure step by step according to a plan which is based on reason. Some students try to memorize the material found in the text or on the blackboard or in lecture notes. If they rely on this means alone they are usually unable in practice in later years to deal with strange situations which are different from those illustrated in the text book.

The Accountant in Conference—Several times a semester, we talk informally before regular classes on the value of a cultivated temperament in business conferences. We encourage students in their discussions among themselves and in classrooms to respect the ideas of others, to control their tempers, to yield only if sound argument shows them to be wrong, to use courteous but convincing language, and to enter any conference for the main purpose of considering all the pros and cons presented, with the idea of emerging with the best solution possible from all the facts presented, and above all not to attend a conference for the purpose of supporting a prejudice. Accountants participate in many conferences. Their services in such conferences are valuable usually in proportion to their observation of these fundamental principles.

An Accountant is Not a Recluse nor a Uriah Heep—Accountancy professors find difficulty at times in convincing vocational guidance experts and personnel bureaus that the professional accountant, if successful, must have a reasonably good personality, must know how to get along with people even though he must at the same time feel there is a possibility of their being ignorant bookkeepers, accountants, or executives, or even crooks. Students are told by us that professional accountants must be good salesmen, must be regularly on the firing line of business, and must be able to make

personal contacts with a variety of people even more than the young lawyer who can stay in his office week after week looking up cases for one of his superiors.

A large measure of the success of an accountant depends on his ability to use tact, diplomacy, and tolerance in all personal contacts while sacrificing nothing in the way of self-respect, principles of conduct, or professional judgment. A professional accountant must of necessity do a large part of his work in the offices of clients where he is observed critically by officers, clerks and miscellaneous employees as to poise, personal appearance, industry, courtesy, work habits, tact and ability to question and even criticize without conveying an impression of condemnation, contempt or undue suspicion.

There are too many so-called educated people who must, outside of office hours, of necessity confine their conversation to their chosen profession or occupation or to baseball, prize fights or the weather. Occasionally, however, one might discuss golf or poker. One should take the opportunity of broadening his observation, his interests, his vocabulary by reading. I am one of those, however, who believe that too much reading can be done at the expense of thinking. Wouldn't it be much better for us at times to pause in our reading and to think things through? There are many times in reading fiction, biography, travel, economics, science, or other fields when one could improve himself materially by thinking of the correlative incidents, events, causes and effects, results and conclusions for an hour or two at a time or by discussing them with others rather than by spending the same length of time in reading. In the last ten years much more good might have been accomplished by congressmen and bureau heads in attempting to pull the country up by its own bootstraps, if more time had been spent in thinking and less in writing and talking.

What direction should our education take after we become certified public accountants, or after we become well established in business? It seems there are four possible points of concentration or, probably more appropriately, points of departure.

1. *Accountants should learn all they can about business customs, procedures and transactions and the economic principles underlying them.* Does not every business transaction, every movement of materials or labor in a factory, yes, practically every minute of time elapsed in a given business, constitute a reason or basis for an accounting entry, which when accumulated with others will yield results that need analysis, explanation and interpretation? Should not the accountant then, who directs the accumulation of such data and supervises their interpretation, understand fully the origin and nature of a great many types of business operations?

The accountant is a practical economist, about in the same sense that an engineer is a practical physicist. The physicist, for example, deals with mechanics of materials, liquids and gases; with heat, light, magnetism, electricity and measurements. The engineer utilizes the principles developed by physicists down through the decades and makes them practicable so that humanity can get the benefit of them. He makes possible our huge dams, tunnels, hydroelectric plants, railroads, radios, airplanes, skyscrapers, all dependent on laws of physics. The engineer must know the principles of physics but must know also how to apply them to human needs. If the engineer knows his physics well, so much the better, but the physicist who is not an engineer falls far short of accomplishing the results obtained by the engineer.

The accountant as a practical economist can be of great service to civilization and to the business world, and to those who are allied with business. He should be fully cognizant of the several essential economic concepts and their relation to society. The accountant, like the engineer, must be practical in his thinking and in his writing. It is easy for one who thinks regularly along theoretical lines to overlook the practical.

Accountants, however, are guilty of impracticality in some respects. Have not accountants for years countenanced the expression $2/10; n/30$ while as a matter of consistency it should be $2/10; g/30$? The two per cent discount is allowed if the invoice is paid in 10 days. If one does not avail himself of this privilege he must pay the *gross* amount within 30 days. Why have we said "net" all these years when "gross" is the real term applied?

Again, why have accountants permitted other misleading terms to arise and obtain recognition with no good result, and, in fact, with no result at all except to add to the confused terminology? Likewise, why is it that accountants, if they are so alert and observing, have not done something to avoid ambiguity in the use of terms which should reveal the direction taken by the one performing a service or executing a transaction? It is very common in a given business to have both interest received and interest paid. But, if, perchance, one wishes to express the fact that interest has been *received* in advance of its due date, one must call it "prepaid" interest rather than "pre-received" interest, just because no one has had the courage to coin this word "pre-received," which would have saved the use of probably millions of other words in the present century that have been used in an attempt to clarify a situation in which the phrase "prepaid interest" appears on both sides of the same balance sheet. Other similar business words and phrases need attention so as to avoid misunderstanding and to facilitate the description of transactions and results.

2. *The accountant should learn much more about government and taxation.* A knowledge of principles of government is not enough to make a good administrative or even legislative official. He must know the practical application of the principles, which application involves proper financial accounting and reporting procedures. It involves balancing of the budget, and an appreciation of the principles of budget making and control. The accountant can be most useful in his community by lending his assistance in such respects and in selecting qualified nominees to run for public office. Although I have mentioned this before in public, without so far observing any good results, why is it that a certified public accountant or one of similar training has never been auditor of the State of Illinois, for example, whose duties include supervision of audits of banks, building and loan associations, credit unions, and other institutions? The position has been held by those from other callings including a bar tender and a farmer, but never by an accountant. Isn't an attorney usually selected for attorney general, and an engineer for superintendent of highways?

There are numerous places in the public service which an accountant is exceptionally qualified to fill. It is our hope that as young accountants find themselves unsuited by temperament, physiques, or other qualities for professional accounting they will make themselves available for public life in some of our bureaus and offices where their business training and their inherent desire for honesty and accuracy will make them most valuable public servants. Such positions exist in nearly all of our taxing bodies. Why shouldn't accountants permit their names to be presented for prominent positions in city, park district, sanitary district, school district, county, state or other divisions of government?

3. *The accountant should learn more about accounting in all its aspects, including the basic elements affected by the laws which relate to the accounting and reporting phases of business.* These include, of course, the laws, regulations and rulings on state and federal taxes, securities and exchange acts, federal power commission, Robinson-Pattman Act, O.P.A., Social Security, and many others, including those dealing with corporations, partnerships, trusts, estates, bankruptcy, and negotiable instruments.

I do not agree with the member of a C.P.A. firm in a city of less than 500,000 population who at a national convention ten or fifteen years ago, in discussing the possible subjects for a technical session, said, "We know all the accounting theory already so let's not have any of that; let's discuss the operation of our offices, the handling of staff members and so on." His was doubtless a worthy proposal from many points of view, but if accountants at that time knew all about accounting they certainly have

forgotten a great deal since then, or the new features arising in the last decade or so have caused them to relegate to the background much of the material already learned. For example, surplus is an old term, an old account, an old balance sheet title. Any member of a C.P.A. board of examiners, however, will say, I believe, that if 100 candidates write on a problem involving several adjustments to earned surplus and capital surplus so that there can be at least 100 different combinations of results, there will be presented in the solutions approximately 50 different amounts for earned surplus; and the author of each result can doubtless refer to some book, periodical, editorial comment, published financial statement or other so-called authority to support his answer. Items other than surplus might also be mentioned as sources of marked difference of opinion. Many have been brought to your attention in periodicals, pamphlets and convention speeches in recent months.

It is very appropriate that accountants should be permitted to use discretion, exercise judgment and have enough freedom of thought to take care of the many unusual combinations of situations that arise, but it seems that there is little justification for a group of intelligent men passing the subject by as one which cannot be improved. Such difficulties as these can be solved within reasonable bounds. Even a partial solution, or the beginning of a solution, requires a great deal of thought on the part of many people, the suppression of considerable stubbornness of some, the ignoring of illogically established precedents, the swallowing of someone's pride, and a more general desire on the part of everyone to do what is best in the long run for business, society and the accountant, regardless of who gets the credit.

It is true that much has been accomplished in the last ten years, and after a few more years of conscientious effort much additional improvement will doubtless be noted. Such improvement should come as a result of the voluntary united action of the leaders in accounting thought and procedure, rather than the mandatory ruling of some governmental regulatory agency.

Although we have referred in large measure to prospective public accountants, we believe that most of the remarks we have made are applicable also to those who are in training for positions in the accounting departments of a business concern. We might say that without much modification they apply also to those aspiring to fill almost any type of position as an executive or junior executive in business.

Obviously, with such a broad program as that just proposed, the process of training an accountant is not confined to four years of college exposure. It is a continuing process, especially with respect to those parts

which arise from extensive reading in general fields and from keeping up with current developments in accounting and its closely allied subjects. It seems, however, that if one is to be educated for most useful service as an accountant one should combine a good general education with a good fundamental education in accountancy. This cannot be done adequately in four years. A fifth year at least is essential in order to furnish the breadth of vision, the sense of proportion, and the historical background of development within the field.

Following are some of the types of subjects which ought to constitute standard equipment for one leaving college as an accountant, but which cannot be crowded into the four years curriculum if the latter includes those basic courses which deal with fundamental principles, develop analytical ability, furnish a perspective of the functions of accounting and of the accountant and arouse curiosity:

(1) Correlation of the several theories affecting the construction or use of various accounts and statements.

(2) A comparative, critical study of the pronouncements in the bulletins of the American Institute of Accountants issued by the Committees on Accounting Procedure and Auditing Procedure, respectively.

(3) A comprehension of the important legal decisions affecting the rights and duties of the public accountant.

(4) A knowledge of the types of legal decisions which have been rendered on accounting concepts, such as depreciation, profits and dividends, and a familiarity with indexes which will be helpful in referring to cases for details when needed.

(5) A general appreciation of the history of the federal income tax laws and the development of their underlying principles with respect to the calculation of taxable income, from time to time.

(6) A critical, historical, and comparative analysis of income tax laws by topics, such as depreciation, consolidated returns, bad debts, capital gains and losses, dividends, tax free income and numerous others.

(7) Some basic studies on what constitutes income from the accounting point of view.

(8) A general study of terminology, not exhaustive, of course, but one which will reveal inconsistencies, ambiguities, and cumbersome phrases. Such a study might be in addition to one dealing with income, cost, value, surplus and other perennial characters.

(9) What is surplus, how many kinds are there and how are they differentiated one from another?

(10) A study from the historical point of view and from the point

of view of good accounting of fixed assets and intangibles and their valuation under varying conditions.

(11) Consideration of the economic, legal, and accounting aspects of consolidated financial statements for affiliated corporations. Also, some research work on best methods of preparing working papers and of handling some items of a controversial nature.

(12) Some historical studies revealing the trend in purpose, form, and content of the auditor's report.

(13) Historical and critical studies of auditing procedure over a period of years, considering effect, if any, of regulatory bodies on such procedure.

(14) A series of case studies on internal check and control.

(15) Treatment of debatable items in the financial statements, such as treasury stock, bond discount, no par stock, appraisals.

(16) Other matters affecting the preparation of financial statements and reports, such as:

- a. Whose statements are they; those of the client or the auditor?
- b. What is the best form and arrangement?
- c. Where shall general reserves be shown?
- d. Can the need of banker and management be served by the same balance sheet?
- e. Limitations on the prospectus as opposed to the statements of a going concern?
- f. To what extent can the accountant express prophecies?

(17) Study of the effect of governmental agencies on accounting and auditing practice and reporting, especially such agencies as:

- a. Interstate Commerce Commission
- b. Federal Power Commission
- c. Comptroller of the Currency
- d. Securities and Exchange Commission
- e. Internal Revenue Department
- f. Office of Price Administration

(18) Ethics of the accountancy profession with respects to others in the profession and with respect to the stockholder, the creditor, the public.

(19) Accounting systems, their adequacy or inadequacy, red tape, budget procedure, over-mechanization, time studies in operation of the system.

(20) Adequacy of governmental accounting systems and procedures; are funds properly segregated and accounted for; are they properly controlled?

There are a number of other subjects to attract one's attention either in formal study at the graduate or undergraduate level or in self-education while one is spending the major part of his time in a public or private accounting position. New applications arise from time to time so that it seems there is always something to challenge one's reasoning capacity and judgment.

We should not close a consideration of postwar training without recognizing the possible effect of aptitude tests on the end results of such training. It might be stated tritely that the quality of raw material in general determines the quality of the finished product. If that be true, then one might say, also tritely, that aptitude tests will contribute to the development of better accountants because more of the naturally qualified individuals will enter the field and more unqualified ones will stay out. This can be accepted as true when, as, and if aptitude tests are designed and results interpreted by those who know, understand, and appreciate all the various shades of duties, responsibilities, and personal contacts required of the accountants; and when such tests can give proper weight to tact, judgment, integrity, perseverance, and industry. Improvements are being made in such tests and examiners are becoming more conscious of their misinterpretations and limitations. We have made some preliminary studies of this subject in cooperation with the personnel bureau and believe that satisfactory results can be accomplished. Accountants must cooperate fully, however, by formulating lists of duties of accountants at various levels of promotion and of characteristics which seem to distinguish successful from unsuccessful accountants. Professor A. C. Littleton, of our staff, has made some initial studies and analyses of such duties and characteristics for both public and privately employed accountants. The American Institute of Accountants has a committee working on the general subject of aptitude tests for accountants.

Summarizing then, training of accountants for postwar responsibilities will follow much the same pattern as that employed by the representative middle western universities in the recent past, including The Ohio State University. General training will continue to be an essential part, but accounting courses should be given in adequate amount to encourage later creative thinking, to develop the ability to reason and to think straight while learning practical principles. Some exposure to office machines and their effect on accounting procedure will be desirable. Changes in formal training of accountants will be necessary from time to time if changes in demands on the accountant seem to justify. One should not overspecialize, but one should obtain enough of the practical to enable him to hold his first

position satisfactorily and reveal a knowledge of the fundamentals which might be expected of a college graduate in his chosen field.

The accountant should develop as far as possible those personal qualities which are so important in his field. The accountant is a practical economist who can and should handle practical affairs of business in the same sense that the engineer is a practical physicist handling a practical application of science. The accountant should not hesitate to train for public service. He should attempt to learn historical backgrounds for many of the present day practices and procedures of accountants, and should attempt to keep abreast of the developments in the field, after graduation, by self-education either through extension service or otherwise. Finally, he should recognize that the accountant is in a better position than anyone else to observe weaknesses in business organizations, customs, practices, laws, and procedures, and to make recommendations for their improvement both for the welfare of the individual business and of society.

CHAIRMAN DOLAN: Thank you, Dean Scovill. Like Professor Paton, you have covered a very broad field in a very short space of time. The thought that comes to my mind is that we have much to learn and not enough time in which to do it.

I was interested in the theory of the aptitude tests, of which you spoke, as a possible aid in the proper placement of people in all branches of the accounting practice and profession.

We have about ten minutes for open discussion.

MR. S. HITNER (Certified Public Accountant, Cincinnati): Selecting from this wonderful menu that has been produced here this morning, I want to take possibly the lighter subject. I am concerned about this question of aptitude tests. I would like to ask Dean Scovill if he would elaborate on that a little more and perhaps tell us something of the developments that have been made in aptitude tests and the experiences he has had in using them with students.

DEAN SCOVILL: I could tell you a little more fully if I had my portfolio. A. C. Littleton of the University of Illinois has taken a great interest in such tests. During the past several months, he has received and analyzed duties of accountants, junior accountants, semi-seniors and seniors, also the managers, in-charge accountants, principles and partners. He has attempted to make these duty analyses available to the personnel departments which interview the youngsters who think they might want to get into accountancy. The personnel people examine applicants and interpret the results in the light of these analyses of duties at the various levels, so that they can tell within reasonable bounds what the personnel qualifications are and whether or not the individuals who apply seem to have the qualities that will enable them to get along well at each of several different levels.

If one shows a strong tendency to be able to handle the duties near the top, and is not so good on duties near the bottom, such as junior accountants, the examiners would probably advise the youngster to enter accountancy work if he shows characteristics for the upper range in spite of his deficiencies in the lower

range. Of course, it is much better if one can show aptitude for handling all those elements well.

The weakness in these aptitude tests so far lies in their inability to interpret or reveal personal characteristics, such as tact and judgment, and similar qualities. We might ask Mr. Carey if he would like to elaborate. He has a committee working on this. Would it be fair to call on you, Mr. Carey?

MR. JOHN L. CAREY (Secretary, American Institute of Accountants, New York): Like Dean Scovill, I do not have my portfolio with me, but I might outline very briefly the project of the Institute that has been referred to.

A committee has raised a fund and has appointed a specialist in psychological measurement and education to study this project, not only for accountants. He is Dr. Wood of Columbia, who has been doing this work for years. As he explains it, briefly, the idea is that over a long period of time, maybe five years, he is to try to isolate the qualities of men who have succeeded at this profession and to see if they can be distinguished sufficiently so that tests can be devised to satisfy the judge as to whether a student or applicant for a job possesses those aptitudes and characteristics which are essential to success.

The difficulty lies in testing for the intangible qualities—character, tact, and judgment. The psychologists have already made a great deal of progress, we are told, in isolating the mechanical qualities. The aptitude tests used in industry have been quite useful, but Dr. Wood feels that by developing a battery of tests, not one, but tests of intelligence, tests of vocational interest, tests of achievement in certain lines of duty, it may be possible after five years' work to develop a set of tests which can then be used on a group of students that can be followed right through their college course, and the early days of their professional careers. He will not feel that he has finished his job until he has succeeded in testing thousands of successful accountants to find out what their qualities are, and then has applied the tests he has developed to thousands of students right through their courses, to find out whether the tests are any good. That is how big a job it is.

CHAIRMAN DOLAN: Thank you. Any other questions?

MR. PALMER W. HANCOCK (Owens-Illinois Glass Company, Toledo): I would like to ask a question of Dean Scovill. He mentioned four year's training and that a five-year college education was really necessary to broaden the viewpoint of the student. I am wondering from the standpoint of the educator if he sees any great change to follow the concentrated programs that have been given to the army and navy students in this period of wartime. I heard Dr. Garry Meyers at Cleveland make a statement a year ago that there would be a change, that the traditional four-year college course would be a thing of the past. I wonder if Dean Scovill agrees with this, in view of his statement that there should be time for thought as well as reading and study.

DEAN SCOVILL: That is the type of question to which I referred in my opening comments, in that universities have many problems of that sort to study over within their own walls. We have given a great deal of thought to that question and have heard it discussed many times. There is a marked difference of opinion, among our own staff and the institutions in general. Some feel that the accelerated courses are here to stay; others feel they are not. Many feel that after the war the students, human nature I might say of the students, will not be very different from what they have been in the past. They will still have student

activities, social affairs, afternoon cokes, if you wish, and athletics and all those things that occupy their attention. Therefore, they will not be in the mood to pursue their courses in an accelerated manner as they have been during the war.

It is probably true that a few elements in the accelerated program might be applied and adopted, but by and large I wouldn't be too optimistic over their results. I am one of those who is more inclined to feel that human nature is going to be much the same after the war as it was before, after we get through the first few years of unsettled situations.

I am not sure that I have considered all the points you had in mind.

MR. HANCOCK: I think, Dean Scovill, I was chiefly interested in it from the angle of the college graduate coming into business and at times the difficulty that he has in adjusting himself to the somewhat concentrated efforts that occur in connection with the business life. Perhaps that is more a matter of aptitude and will come out of these aptitude tests and reaction and interest.

DEAN SCOVILL: I might add just one more remark. These accelerated programs have been reasonably successful although I understand some of them have not been. We appreciate, I believe, that these accelerated programs have been offered to men with a very definite purpose in mind, a very definite goal before them. Also, such students are more mature, and they recognize a certain element of possibility of promotion or lack of promotion beyond the accelerated program.

It seems to me that they have had a number of incentives to study hard, foregoing all social life and athletic life, and so on, which the students in normal times will not have. Lack of incentive I think will be one of the greatest elements to make it difficult to apply those accelerated programs as they have been applied during the war period. We might apply some of those ideas but I doubt if we should apply all of them.

CHAIRMAN DOLAN: Do you care to express your opinion on that question?

MR. PATON: I have a feeling that we may compromise in the postwar period between the practice of the past and the experiments we are trying now and perhaps have a semi-accelerated program. I think we have, in the past, wasted a lot of time with the educational process. We waste it in the secondary schools and in the university. It is perfectly ridiculous to take more than three calendar years for what constitutes an ordinary high school program at the present time. Years ago many high schools made it feasible for a student with any ability to get through in three years, and I think that a year could be salvaged from the high school program very generally. The government may take that year and have the student in the army. I expect to see some attention given that question in the secondary schools.

When you come to the college level, I think that could be done in three years very well. In other words, we could just as well save two years, one in high school and one at college, if you are thinking of going through a general extended program before going into professional work. At the same time, I would agree we are not likely to keep the students on the continuous treadmill they are on at the present time, and I think certain, definite things are lost when that is attempted. The time element is important in education as well as the effort and concentration element, but I hope we will try something by way of a compromise on the question.

Now that you have given me a chance, I might say a word on the aptitude test. I do not want to strike too sour a note. I am in sympathy with the experiments that Secretary Carey of the Institute has described here for us. The way to find out about these things is to go after them. But we must not hope for too much. I remember reading an article in the *Readers' Digest* not long ago about the experience of a chap, a mechanic who had been in Egypt charged with the task of developing some decent tank and truck repairmen from the supply of Egyptian peasants or "fellahs." He had a simple rule. His theory was that there are just two classes of people: the "bright-eyed guys" and the "dull-eyed guys." He lined up a couple of hundred of these unwashed fellahs and he looked them over from that single standpoint and picked out about 35 or 40 of them, and about three-quarters of those he picked out he turned into pretty good mechanics.

I think we can tell something about the native abilities of a person by ordinary tests, and I think that is about as far as we can go. We can pick out those who have a high level of capacity from those who have less capacity. You can't tell much about the intangibles and imponderables and you can't do much about the luck factor that enters into success to such an extent. I wouldn't trust a psychologist—any I have ever seen—to take a bunch of freshmen in college and pick out the ones who ought to go into accounting and the ones who ought to go into something else. Generally speaking, all the bright chaps could do a number of things well. About all the tests can accomplish is to select the group of people who are the best prospects for all advanced lines of training.

CHAIRMAN DOLAN: I think we could get into an argument here very readily, particularly as accountants. We might be a little depressed in the course of the remarks, but we feel a little important when we think of the things that could be covered by accountants. That might be good for us.

On behalf of The Ohio State University, myself, and all those present, I thank Professor Paton and Professor Scovill. If time permitted, I know that many interesting discussions, occupying all of us for several days, could be developed from the many thought-provoking remarks made by each of our speakers. It is my hope that they will appear on many future programs.

SECOND SESSION

FRIDAY, MAY 19, 1944—2:30 P. M.

Commerce Auditorium

Chairman:

GRANT R. LOHNES, *The National Cash Register Company, Dayton*

Address: "The Nature of Postwar Accounting"

VICTOR H. STEMPEL, C.P.A., *Touche, Niven and Company, New York;*
President, The American Institute of Accountants

Address: "The Nature of Postwar Accounting"

LOGAN MONROE, *Controller, The Eaton Manufacturing Company, Cleveland*

INTRODUCTORY REMARKS

By RUSSELL S. WILLCOX
Accounting Department, The Ohio State University

and

By GRANT R. LOHNES
The National Cash Register Company, Dayton, Ohio

MR. WILLCOX: Mr. John H. DeVitt of the Hammermill Paper Company, of Erie, Pennsylvania, who is president of The National Association of Cost Accountants, and who was to have presided this afternoon is unable to be here. In his place we have Mr. Grant R. Lohnes, of The National Cash Register Company, a past president of the National Association of Cost Accountants, who will preside.

CHAIRMAN LOHNES: We have a very interesting subject this afternoon, "The Nature of Postwar Accounting." I wonder sometimes whether that was the subject we should have used or whether it should not have been "The Postwar Nature of Accountants." I think sometimes the nature of accountants has more to do with the success of accounting than conditions existing at the time.

I was thinking this morning when we were hearing some controversial points raised on the subject of accounting, whether it wasn't just about time that we accountants began to agree on some particular points and use that agreement as advice and guidance to our clients, and not only to our clients but to our employees as well.

Now I am not going to engage in a long discussion on any of these subjects because the two speakers that we have this afternoon are certainly well-fitted to discuss this subject.

Our first speaker is Mr. Victor H. Stempf, of Touche, Niven and Company, New York. He is the president of The American Institute of Accountants, and past president of The National Association of Cost Accountants. Mr. Stempf.

MR. VICTOR H. STEMPF: Mr. Chairman and Fellow Accountants: Were it not for the fact that I have a rather heavy chest cold, I should like to take most of my time in rebutting some of Bill Paton's usually provocative statements. One of them I must deal with (my secret boast to myself alone): regardless of what little I may have learned about accounting, I

still consider myself a damn good auditor. Furthermore, I think that if you question any of the men in public practice, they will tell you that what they may have accomplished in accounting or otherwise in the profession, they owe to that exacting training which they got in the very beginning by following auditing procedures. I won't labor the subject.

THE NATURE OF POSTWAR ACCOUNTING

By VICTOR H. STEMPE, C.P.A.
Touche, Niven and Company,
President, American Institute of Accountants, New York, New York

There are many who assert that it is still too soon to sing: "Where do we go from here, boys?" Your boy and mine at the front wrongly view our interest in the postwar era as flagrant evidence of a detached and heartless indifference toward the suffering and stark brutality which they endure.

Let there be no mistake! Both at home and abroad, a maximum war effort remains essential. The zeal of that effort must continue unabated. The foe must be crushed to enable our armies to return home safely to help in winning the peace.

The rigors of a planned and regimented war economy have carried us beyond the horizon of our customary way of life, and the return to peacetime pursuits and production will challenge the will and ingenuity of all of us to hold fast our American ideals. The recapture of our way of life will demand a maximum of courage, cooperation, and competence. It must be quickened by freedom of opportunity.

The Measure of Postwar Prosperity

Jobs in private industry will be the barometer of postwar prosperity! These postwar jobs must be productive and well paid. Attention must be focused on high output. We must not be misled by the false Utopia of shorter hours which Phillip Murray calls "concealed unemployment." Only by producing more can we improve the common lot.

Vital steps in the orderly resumption of civilian enterprise will include the demobilization of the armed forces, the transfer of some twenty million workers from war work to civilian occupation, the settlement of cancelled war contracts, the disposal and conversion of war inventories, and the reconversion of war plants to peacetime production.

Carrying through this tremendous transition program will entail a momentary sharp decline in the production index. Fortunately, we shall have at the end of the war an accumulated demand for civilian goods equal to at least two and one-half years normal business. This demand, coupled with the reconversion and retooling of plants, and the great unfilled need for housing, afford the basis for a well-rounded and self-sustained prosperity.

Although these vital problems of the transition demand our best attention and are engaging most of our time now, they have no place in this discussion. The forums and literature of the American Institute of Accountants, the State Societies of C.P.A.'s., the National Association of Cost Accountants, and other accounting organizations are contributing generously to the development of the underlying philosophy and the practical administration of these problems. Many of us have an active hand in these developments.

Postwar Planning

Nor is it my purpose to discuss postwar planning, concerning which many reassuring activities are under way. It is self-evident that if business is to have a clear road for the enlargement of postwar production, sales, and employment, it must be ready with its postwar plans; and it must recognize the obligation to think in terms of all business, the public interest, and, particularly, the interests of the workers.

Sound planning and budgeting are clearly recognized as the pillars of orderly business conduct, and it should be emphasized that no other phase of accounting has the same predominant importance. Accountants, whether in academic, industrial, or professional work will render their most valuable service to the reestablishment of a stable and secure economy through the development, dissemination, and application of their highly specialized knowledge in this field. The most urgent injunction to accountants today should be to refresh and extend their knowledge of the modern accounting techniques concerning standards and budgets. Intensive refresher courses in the colleges, forums in our accounting societies, writing, and speaking on these subjects are the first order of the day. The plans of management are primitive, vulnerable, inadequate, and dangerous unless implemented by these invaluable tools.

Burdensome Regulation and Regimentation

The all-out war effort has required the enactment of many emergency measures imposing artificial and arbitrary controls to divert and concentrate the national resources and vigor into war production. When the emergency ceases, when the excuse and reason for these burdensome administrative laws and bureaus no longer exist, Congress must help the people by promptly repealing every law enacted solely for the purpose of implementing the war effort, because such repeal will foster the normal means of support of business in its broadest sense.

In this same category, it is self-evident that needless complexity and uncertainty of burdensome and confusing Federal tax laws are anethema in

a business world harassed by myriad unavoidable economic problems. The need for tax reform and simplification is universally recognized.

Business leaders and leaders of the accounting profession who have lived with regimentation are capable of soundly interpreting the nation's needs in this respect. Certified public accountants have contributed much toward relative simplification and workability of the interwoven pattern of many of these measures. The profession will make an equally valuable contribution to the unravelling process. All accountants should exert the full measure of their influence to encourage Congress to pursue diligently a sound program to implement the orderly resumption of civilian enterprise.

This purge cannot be effected in one fell swoop; the limited retention of some of the war measures may be advisable to supplement legislative dealing with termination of war contracts, disposal of war materials and facilities, and other demobilization problems; but there must be a constant constriction and ultimate eradication of these emergency measures.

Evolving Economic Concepts

It seems folly to believe that we shall resume the type of rugged (sometimes ruthless) individualism which broadly characterized the growth of our nation. It seems equally obvious that we must retain the sound framework of private enterprise and initiative which has made possible the magnificent accomplishment of our people.

That framework contemplates sustained high employment, vigorous private enterprise encouraged by effective incentives to the assumption of risks and responsibility, complemented by cooperative activity of the legislative and administrative branches of government in fostering fiscal programs of taxation and expenditure to mesh with private undertakings, fostering a stable economy. This is not a planned economy in the sense of government as the Master of the People. It is rather intelligently planned cooperation whereunder government remains the Servant of the People. The financial operations of government should harmonize with the activities of private business to maintain an effective demand adequate to sustain high levels of employment at sound price levels.

Such a policy does not condone mere wasteful spending. It does contemplate that over-expansion of private business activity may be restrained by public debt retirement, or that purchasing power and private enterprise may be stimulated through reduction of tax rates. Similarly, public works should be planned and timed to provide a reasonable level of construction over a long period; not that it can accomplish much in leveling out the whole business cycle but that it certainly can even out the activities of the construction industry itself.

The public works program should be planned on a clear basis of economic and social utility, not on that of mere fiscal or political opportunism. The tax program and the public works program should go hand in hand with business in a general attack on mass unemployment.

American taxation has been characterized by fiscal and political opportunism without coherent long-range planning. Postwar taxation must be more purposeful, particularly to give favorable environment for the soundest possible peacetime economy. Once the framework of taxation is redesigned, it should be kept stable, simple, and understandable. Changes in rates thereafter should come only in response to changing fiscal needs.

So much for the backdrop of the stage upon which our postwar drama will be enacted. Within this setting, what will be the nature of the problems of postwar accounting?

Essential Importance of Accounting

With startling speed, particularly during the last two decades, accounting has become a potent social force in the interpretation, direction, and control of our evolving national economy. As the government has extended its control and supervision over economic activities, it has become more and more apparent that accounting is an important instrument of regulation. It has clearly demonstrated its value as a management device under a free enterprise system. It is equally evident that it will continue to be of great importance under any system of relationship between government and business. Through one emergency after another it has manifested its ability to meet new tasks and new conditions promptly and satisfactorily. There is no reason to doubt that it will meet its postwar challenge competently.

Postwar Accounting Problems

Previous reference has been made to the major task of accounting in the postwar period. This should be reemphasized. The redetermination of standards, further development of distribution cost techniques, broader and sounder application of the principles of differential costs, and a wider appreciation, dissemination and application of sound budgetary planning and control, assure a field of inestimable value for postwar accounting, within which it may wield an important influence in the redevelopment of a sound and stable economy.

These techniques answer admirably those pressing problems with which management will be confronted. Management asks: "If we resume our prewar production, or if we enter new fields, what markets shall we enter, how much shall be produced, what normal capacity will be required,

what facilities of production will be needed? Is there adequate economic justification for substantial expansion of capital expenditure; what will our costs, selling prices, and profits be; what are the utilization values of existing facilities under the projected program?"

Standards and Budgets

None of the foregoing questions can be satisfactorily answered without integrated accounting forecasts. Once the program is set, the effectiveness of accomplishment cannot be adequately measured and controlled without being related to predetermined standards of performance, affording the key to causes and amounts of variances, thereby providing the basis for remedial measures. More and better goods at lower prices must be the slogan of the postwar economy. Cost reduction through improved efficiencies and technology will tax the resourcefulness of postwar management. No better instrumentality of analysis, interpretation, and control is known than that provided by modern accounting techniques which focus attention upon elements of exception, made possible by the scientific correlation of promise and performance.

Every accountant in the academic, industrial, and professional fields owes it to himself to intensify his research in these areas, and to contribute to the fund of common knowledge by exchange of ideas, through discussion and writing in any one of the many avenues open in accounting circles.

It is self-evident that in the future, as in the past, accounting will render its most constructive and valuable service in the field of sound advice to management; advice in the sense of providing those media of analysis and interpretation of transactions which afford sound guidance of policy and reliable bases for future management action.

Financial Reporting

Previous reference was made to accounting as an important economic and social force. As the hand of regulatory commissions extends into the control of business, the vital importance of sound accounting magnifies. Let no one underestimate the importance of accounting in the field of financial reporting. This relates not only to mandatory reports of regulatory agencies, but also to reports to stockholders on the stewardship of management, and representations to credit grantors and prospective investors.

In all of these fields, the enterprise makes the primary representations, and the independent certified public accountant expresses an opinion concerning the fairness of such representations. Modern practice demands that these correlated representations and opinions shall be predicated upon audits

conducted in accordance with generally accepted auditing standards, and that related financial statements shall have been prepared in accordance with generally accepted accounting principles consistently applied.

Now, just what are generally accepted auditing standards and generally accepted accounting principles? Many people continue to assume that financial statements are made up by precise and mysterious formulae which result in completely accurate expressions of fact, which the average citizen thinks of in terms of his own salary and bank account, that is, as cash in hand.

Cost vs. Value

The failure to comprehend that accounting is essentially not an expression of values but is a conventional method of apportioning costs to past, present, and future periods, and the further failure to understand the large factors of judgment and opinion affecting accounting decisions, not only mislead the public in forming opinions of the results of business activity, but also results in failure to appreciate fully the great value of the independent confirmatory judgment of the C. P. A. concerning the representations of others in respect to such financial statements which are a mixture of fact, estimate, and approximation.

This confused and uninformed attitude carries over into the legislatures of our states, into our national Congress, into courts, juries, and regulatory bodies. Neither the public nor its lawmakers realize the importance of accounting and financial statements in the formation of policies of greatest significance to the nation. Nor do they apprehend the far-reaching influence of accounting rules and decisions upon business transactions, the payment of dividends, the scale of wages, the liability for taxes, and myriad other impacts of accounting upon the lives of all people.

These are aspects and implications of accounting which must be diligently pursued in the postwar period. This uninformed indifference of the general public and of those who represent it endangers the public interest. Without premeditation, it might permit enactment of legislation which would weaken and perhaps obliterate some of the most useful functions of financial reporting. It is of vital importance that public opinion be informed, and, to this end, the American Institute of Accountants, with invaluable cooperation of State Societies, has carried on a persistent campaign to bring information about accounting to the public. This field of public relations is most interesting and complex. It poses one of the large problems of the profession in the postwar period.

Accounting and Auditing Standards

The leadership of the accounting profession in setting the standards in accounting has been challenged in some measure by the regulatory agencies of government. The bodies have handed down decisions in some cases, enunciating so-called accounting principles which the profession does not regard as generally acceptable. The work of formulating high standards which can be generally applied is greatly handicapped by these intrusions.

In a recent utility case before the U. S. Supreme Court, the Institute filed a brief as friend of the Court. The Federal Power Commission, having declared it necessary for the company to eliminate from its capital investment accounts a large amount of "aboriginal" appreciation, found itself in a quandary as to how the elimination should be handled. An immediate write-off would have impaired surplus. It seems that, as a matter affecting the public interest, the Commission did not want to stop the payment of preferred dividends. Therefore, it came to the ingenuous conclusion that sound accounting required the elimination to be effected by annual charges against operations to the extent that such annual earnings exceed the preferred dividend requirement.

If, as an expedient of social reform, the Commission wants to issue such a ruling, the profession has no voice in the matter, but when the Commission bases its conclusion on the assertion that the ruling follows sound accounting, the profession cannot remain silent.

The Supreme Court sustained the Commission, saying:

Although as suggested in a brief filed by the American Institute of Accountants the Commission's prescribed method of eliminating the write-up may not agree with the best accounting practice, it is sustained by expert testimony. It is not for us to determine what is the better practice so long as the Commission has not plainly adopted an obviously arbitrary plan.

It is apparent that the Supreme Court did not consider the Commission's plan "obviously arbitrary," and it should be noted that the testimony referred to is that of the Commission's own experts. Unfortunately, there is now precedent in the law of the land which condones this absurd distortion of sound accounting.

A statement made some time ago by A. A. Berle, Jr., now Under Secretary of State, is pertinent to the subject:

Every administrative body has a specific job to do, and serves a special interest. That is why it is here. Its views on accounting, accordingly, are conditioned by its desire to reach that result, rather than by any interest in the healthy growth of accounting as a whole. . . . There is always danger where accounting rules are made by specialized administrative tribunals, that the resulting body of doctrine may be lopsided, if not positively dangerous, however

conscientiously the rulings have been made from the point of view of the administrators making them.

The American Institute of Accountants is engaged in a vigorous endeavor to bring the conclusions of regulatory bodies on accounting into line with the best thought of those who make accounting their profession. Research, discussion, and writing for publication are indispensable in the development of any profession. The Institute has fostered these activities for many years, which evolved into formal Accounting Research Bulletins in 1939.

In the first of these bulletins issued in September, 1939, the Institute's Committee on Accounting Procedure reiterated certain rules previously adopted by the Institute, and has, from time to time, issued some twenty timely additional bulletins dealing with generally accepted accounting principles.

As far back as April, 1917, the Institute collaborated with the Federal Reserve Board in the preparation and promulgation of a bulletin entitled, "Approved Methods for the Preparation of Balance Sheet Statements," of which the bulletin, "Examination of Financial Statements," issued in 1936, is a revision. These bulletins deal largely with generally accepted auditing standards; and, as in the case of the Institute's Committee on Accounting Procedure, the Institute's Committee on Auditing Procedure began the formal issuance of bulletins in October, 1939. Some twenty of these have, likewise, been issued to date.

These activities are implemented by the Institute's Research Department, which, in addition to these formal pronouncements, will shortly begin the issuance of studies of the discussion type, not necessarily reaching conclusions, but fostering broader debate to hasten the formulation of authoritative standards. Back of these authoritative pronouncements of generally accepted accounting principles and generally accepted auditing standards there lies an impressive native professional literature comprising much that is generally accepted and some that remains unsettled. The acceleration and extension of research projects, too, will be one of the major objectives of the profession in the postwar period.

Trend of Research

The trend in the last few years in research has been directed toward greater objectivity in both accounting and auditing problems. Whether a principle is generally accepted is primarily a question of fact rather than opinion, and the conformity of financial statements to generally accepted principles must be determined in the light of objective criteria, and not according to what the accountant or any one else may happen to think is

sound or acceptable. While objective standards, and not the views of the individual (subjective opinion), are the deciding factor, there still remains ample scope for professional judgment in selecting the rules or principles which have controlling applicability, and in deciding the manner and extent to which they shall be applied.

Evolution in the determination and application of accounting principles results from determined sponsorship of change on the ground that proposed practice is sounder, even though not generally accepted at the time. But until the majority has been convinced, the majority view should control as to what is generally accepted. To substitute subjective, personal opinion for the objective standard constitutes a distinctly retrogressive step and fosters chaos. If what is generally accepted is unsound, the strength of opposing argument will quickly make itself felt.

We are entitled to expect of regulatory bodies the same objective approach which we establish for ourselves, and to which they properly hold us.

Straight-Line Depreciation

For example, however wise the exclusive use of straight-line depreciation might be for regulatory purposes, accountants should be greatly concerned if it were made a requirement on the ground of "sound" accounting, with the implication that other accepted methods of providing depreciation are unsound.

Amortization of Goodwill

With increasing frequency in recent years, the question is asked whether "sound" accounting requires goodwill to be amortized against income? Most accountants have held the view that, from a going-concern standpoint, there is no occasion to write off such goodwill if it continues to exist. On the other hand, if for reasons of conservatism or otherwise, the company wishes to eliminate the goodwill, accountants generally would interpose no objection, provided the result were accomplished by an appropriation of income or earned or capital surplus, as distinguished from a charge against profits.

Such a write-off, where there has been no permanent impairment of earning capacity, should not be construed as an acknowledgment of loss incurred, and may with propriety be charged against capital surplus, if such surplus exists. On the other hand, where permanent impairment of earning power is evident, there may indeed be some question as to the propriety of continuing to carry the goodwill on the balance sheet.

Generally, the proponents of the amortization theory do not argue

from the premise that goodwill is not a valuable asset or that it does not constitute property, but rather on grounds that goodwill may disappear; that profits arising from goodwill purchased do not accrue until after the purchase price is recovered; that original goodwill disappears and should be amortized although it may be replaced by new goodwill.

True enough, those expenditures which maintain goodwill must be continuous in any organization which expects to enjoy sustained public support. Sales promotion of all types, research and development, costs of public, customer, and employee relations, and all similar expenditures create future benefits in the sense of maintenance and development of earning power and goodwill. Accountants generally concur that these should be absorbed currently. Consistent with the goodwill amortization theory, they would have to be capitalized for future amortization, otherwise there would be a doubling up of charges resulting in an understatement of income. To do so, however, would simply inject procedures more difficult in practice which, probably, would produce substantially the same result.

Whatever other motivation there may be for sponsoring the amortization of goodwill, we become directly concerned when the change is attempted on grounds of "sound" accounting; and it becomes a question on which we are entitled to be heard and to speak with authority. Accounting decisions should be based on objective criteria, and should not be induced by preconceived objectives, however praiseworthy.

Capital Surplus

More difficult of solution is the provocative subject of the status of capital surplus and the related question of the propriety of charging premiums paid on capital stock reacquired against such surplus. We need to agree whether the corporation's capital and capital surplus is that of the business as an entity separate from its stockholders (which in my opinion is orthodox), or whether the paid-in surplus remains permanently apportionable to the different classes of stockholders who contributed it, which seems to inject an unwarranted partnership theory into corporate accounting.

Federal Income Tax Treatment

Again, in respect of the treatment of income taxes, differing opinions have waxed with the increasing importance of taxes in financial reporting. The subject remains unresolved after many months of debate in the Committee on Accounting Procedure. Are Federal Income Taxes an operating cost or the share of profits payable to the dominant partner, the government? Notwithstanding that these taxes are so high as to make profits before taxes

the item of outstanding importance in judging results of operations, it seems elementary to me that profits start where costs end; that it is utterly repugnant to view government as a partner in private enterprise; that in essence these income taxes differ in no sense from all other types of taxes; that in free enterprise they inevitably enter the price structure to the extent that competitive markets permit; and the dollars used to pay them come from the same sources of income that provide the means to pay wages and all other types of cost and expense. We do not reach an amount to be described as profits until all costs have been deducted, and that which remains distributable to stockholders is entitled to the designation of profits, and not before.

Do the gross incongruities between corporate income and taxable income render ineffectual any attempt to match costs against revenue insofar as income taxes are concerned? Should the nonrecurring nature of tax charges and credits be recognized and sharply distinguished?

When a carry-back occurs does the event stem from the higher profit of the earlier year or the loss of the later year, and does the adjustment affect the current year's income or that of the earlier year? Should the fortuitous circumstances attending the incidence of taxes be ignored and merely the fact of the amount payable be recognized? If so, should the relation of taxes and tax adjustments be shown among operating charges or should they be deducted from profits before taxes at the end of the statement? Should they always appear in the latter position in the year of determination or should we attempt to relate them to the past, present and future years, by involved allocation between income, surplus, and reserves?

The causes and effects of material tax adjustments are certainly material facts requiring disclosure, but whether appropriate disclosure extends to complicated apportionment to past, present, and future years remains a debatable subject. These allocations can in many respects be as complex and arbitrary as in the case of the obvious example of an additional assessment against a series of prior years. These are often based upon "horsetrading," and the final determination is an aggregate and unallocable sum which, at best, may be appropriated on the basis of arbitrary assumptions.

Fundamental Philosophy of Accounting

The foregoing examples of pending questions suggest that some of these specific questions must be related to more basic questions concerning the underlying philosophy of financial statements, their character and function; whether they are purely historical, or whether they should implement appraisal of the future and thereby partake of the nature of a

prospectus. As these questions evolve and crystallize, solutions of many other questions will be found which will merit general acceptance.

As the Committee on Auditing Procedure pursues its studies, it becomes more and more evident that generally accepted auditing standards are governed by three prime considerations:

- (1) The relative materiality of an item.
- (2) The relative danger of material errors whether of omission, commission, or judgment.
- (3) The limitation of cost to the area of prudent economy.

Thus, in the case of the bulletin dealing with direct communication with debtors of public utilities, the discussion centered around the degree of internal control exercised over the mass of accounts receivable. The conclusion, in the case described, recognized sufficient separation of duties to assure substantial accuracy and to prevent significant irregularities. Accordingly, under the system of internal control prevailing, the mass accounts receivable should be considered reliable for financial statement purposes. Test confirmation of the mass receivables was not deemed necessary to check the credibility of the company's representations as to their authenticity, but a small sample or test circularization was advocated as an additional check upon the functioning of internal control.

This is a clear example of the effect upon the audit program of conclusions concerning the relative risk of material error. Let me repeat that the test circularization was clearly intended as a check upon the effectiveness of internal control, and not for the usual purpose of checking the credibility of the company's representations as to the authenticity of the mass accounts receivable balances.

Thus, in both the sphere of accounting and auditing the answers to pending questions seem to rest upon certain broad general philosophical principles which apply throughout. Finding these underlying guideposts is one of the major problems of research in the postwar period, to hasten the development of a unified and coordinated body of theory in both accounting and auditing.

Independence, Advice, and Advocacy

Another challenge confronts the accountant in professional practice in the postwar period. I refer to the maintenance of his professional status as an *independent* Certified Public Accountant.

Accountancy in the United States has made an irrevocable choice of the professional status, which carries with it valuable privileges. It confers upon the holder social recognition and prestige which broadens his opportunity for service. In return, the public expects the members of the

profession to maintain standards of competence and integrity which will assure honest and able service to the public.

The professional status carries a far greater responsibility than that of merely rendering competent technical service. It imposes the responsibility of exercising independent judgment, a sense of responsibility to others than those who pay the bill, a subordination of desire for profit to the obligation of service to society as a whole. This is not said in the spirit of the moralist who tells us to be good for the sake of being good, nor in any spirit of pride, but in a normal practical spirit, in the belief that enlightened self-interest demands acceptance of what Dr. Wickenden describes as "conscious recognition of social duty." The acceptance of that responsibility to the public vests the opinions of the independent C. P. A. with a dignity and corroborative value apart from and in addition to the value of the representations of those whose accounts are examined.

Recent opinions of the Securities and Exchange Commission seem to challenge the independence of C. P. As., for purposes of expressing opinions on financial statements filed with the Commission, if the accountant has been closely associated with the management of the enterprise as an advisor on accounting policies, or has participated extensively in interpreting transactions, and in devising related entries in the books of account, or if he has acted for the company in a manner considered that of an advocate, such as arguing tax matters before the Bureau of Internal Revenue.

The American Institute of Accountants does not accept this point of view. It insists that the professional accountants whose reputation for integrity and objectivity is his principal stock in trade can be and is independent in expressing his opinion regardless of other services performed.

The published rule of the S. E. C. has been modified in form to provide that in determining whether in fact an accountant is independent, in respect of a particular registrant, the Commission will give appropriate consideration to all relevant circumstances including evidence bearing on all relationships between the accountant and the registrant.

There have been other attacks on the independence of professional accountants, regarded as of gravest importance because independence is viewed as the keynote of our professional capacity. A senator recently questioned whether professional accountants may properly act on behalf of the government as independent auditors in reviewing claims submitted by companies among whom their own clients may be found. A question was raised in Congressional committee in respect of Price Adjustment Boards accepting financial statements certified by the professional accountants regularly retained by the contractor. A branch of the War Department,

while expressing a willingness to accept reports of independent auditors, submitted to them by contractors, questioned their own right to name as accountants, for investigations made for the War Department, the same accountants as those regularly employed by contractors.

All of these instances were promptly met and rebutted by correspondence and interview, with satisfactory corrections of the record; but in this area, too, much more remains to be done to crystallize public opinion. Certainly the accountant should not surrender his professional independence in dealing with regulatory bodies and other government agencies. He is expected to express his own unbiased opinion, based on an examination conducted in accordance with generally accepted auditing standards, and determined in the light of generally accepted accounting principles. His own opinion is required, and not one influenced by someone else, however authoritative that person may be.

On the other hand, the professional accountant should not be unduly swayed even by his own personal views, when he has reason to believe that his personal views differ from those of the majority. Thus, he may deem it futile for accountants to attend and observe the taking of inventories. He may believe that depreciation charged against income should be based on cost notwithstanding the fact that the assets may be carried at appraised values higher than cost. He may not agree that it is proper to carry forward premium on redemption of bond issues which have been refunded.

These are matters on which honest differences of opinion are possible. Nevertheless, respecting questions such as these on which the profession has taken a position an accountant could not say that he had complied with generally accepted auditing standards if he had not undertaken the required inventory procedure, nor could he expect his personal views to prevail against accounting principles which are generally accepted. The burden of proof would be upon him to defend any departure from them. He might believe his views to be sound and acceptable, but it would be difficult to show that they were generally accepted.

The term "Advice" comprehends all assistance to management in planning and interpreting operations, system work, strengthening internal control, interpretations and recommendations on all matters of accounting, finance, and business policy. These are all usual and proper professional services.

Advocacy contemplates representation of a client in controversies involving accounting. This arises primarily in tax matters, though more recently it has occurred also in renegotiation and termination matters. These extensions of attempted advocacy are viewed with some alarm, as they

cannot do other than undermine the public acceptance of our chief stock in trade—our independence.

Conclusion

The roots of the C. P. A's usefulness lie in his independence. If he is not independent of his client, he is of little use to stockholders or credit grantors. If he is not independent of credit grantors, his usefulness to his client is impaired. If he is not independent of regulatory commission he cannot properly discharge his responsibility to others. Our value to the economy, and our greatest postwar opportunity for service lie in our ability to serve as impartial interpreters of financial results of corporate operations.

The question should be discussed and debated at length. When debate has cleared the air, an attempt should be made to state the profession's position in unmistakable terms—perhaps as a rule of professional conduct—to resolve the doubts in the minds of responsible representatives of the public.

It seems clear that whatever the future may hold, the key to professional stature and usefulness lies in the retention of the fullest measure of independence.

CHAIRMAN LOHNES: Thank you very much, Mr. Stempf. We have heard Mr. Stempf talk on the subject for this session from the public accountant's viewpoint. Our next speaker is Mr. Logan Monroe, Controller of the Eaton Manufacturing Company of Cleveland, who I think is well qualified to speak on the subject from the industrial accountant's viewpoint. Mr. Monroe has had long industrial experience. Mr. Monroe.

THE NATURE OF POSTWAR ACCOUNTING

By LOGAN MONROE

Controller, Eaton Manufacturing Company, Cleveland, Ohio

You are about to hear the anti-climax to end all anti-climaxes. It is futile to attempt to gild the lily. When any speaker attempts to share the same platform with my good friend, Victor H. Stempf, he starts under two terrifically large handicaps: one, intellectual; the other, physical. It would be a tough enough job if the other speaker had an entirely different subject, but when, as today, I have to talk on the same subject, the prospect, to say the least, is far from inviting. It seems that your program chairman felt that an industrial accountant might perhaps pull the session down to something approaching a mundane level and I was selected as the sacrificial offering.

There are, however, some compensating factors for an industrial accountant who has the temerity to appear before an Institute such as this. The public accountant is constrained by a sense of professional responsibility and the teacher of accounting must observe certain standards and canons, but the industrial accountant has no such inhibitions. He can look with suspicion and view with alarm to his heart's content without being held to any strict accountability other than that of his own conscience, which at times may be of doubtful quantity and quality.

I have been asked to talk on the nature of postwar accounting. To me the word "postwar" implies two things: planning and prophecy. Even before Pearl Harbor we were beginning to hear of postwar planning and for some eight or nine years prior to that time we heard a lot about planning—just planning. During that eight or nine years, I had become a little tired of planning and the planners. I might even make it a little stronger and say that I had become definitely suspicious of their infallibility and also of their objectives.

When conditions were good and there was a fair degree of prosperity, it was said, "We planned it that way." On the other hand, when the machinery started to creak and groan and slow down, it was because the money changers and economic royalists had thrown a monkey wrench into an open gear box. The planners, it seemed, in a momentary fit of aberration had inadvertantly left the gear box open and the big, bad businessmen had

seized the opportunity again to stop the wheels of progress at the expense of that well-known one-third that is ill-fed, ill-clothed, ill-housed. After so long a time, such a pattern became definitely monotonous.

Now for the last two or three years, something new has been added. Postwar! What a word for the professional planners! Perhaps in an equal space of time more has been written and spoken around that two-syllable word than any other word in history. And, seriously and regretfully, I must say that, in my opinion, it has been, for the most part, just words. Formerly, the planners were usually the starry-eyed boys. Now it's an open field. Little businessmen, big businessmen, labor leaders, economists, politicians, and, of course, the original professional planners, all have their plans, but the great majority of these plans are based on the principle that self-preservation is the first law of nature. The main difficulty, however, is that each group wants to be preserved first.

Perhaps by now you are beginning to think that I believe there should be *no* postwar planning. That is definitely not the case. Naturally, there should be planning not only for postwar but always. Budgeting is planning. However, I think we could do with a lot less talk and a lot more real planning. Now it is easy for me or anybody else to get up and hand out a lot of destructive criticism concerning postwar planning and you might well ask what constructive ideas, if any, I may have. That's a good and fair question and perhaps I have a poor answer.

Mr. Paul Hoffman of the Committee for Economic Development thinks that the solution is for each community and each individual enterprise to do its own postwar planning, and from that effort there will grow an integrated plan which being good for all the parts will be good for the whole. With that idea I am in hearty accord, but I should go one step further, and, probably this is implied by Mr. Hoffman, let each individual, insofar as it is humanly possible, endeavor to plan his own little postwar future. Perhaps that is pretty visionary but I think it is a lot less so than a great many other plans that have been proposed in all seriousness, and recommended to cure the ills of the entire economy.

Having now demonstrated to your satisfaction that I am not much of a postwar planner, perhaps I should try to get back to the subject to which I was supposed to confine myself, namely, the nature of postwar accounting, with respect, particularly, to industrial accounting. As I said earlier, the word postwar, among other things, implies an element of prophecy. In fact, most of what has been contributed to date on postwar planning is more wishful thinking and prophecy than definite planning. Only last Sunday evening that well-known economist and statistician,

Walter Winchell, announced that for five years after the end of the war there would be more jobs than there would be people to fill them. I hope he is right, and he is probably as well qualified as a great many of the prophets who have burst into print.

However, a certain amount of prophecy must be attempted, and in order to discuss the future of industrial accounting, or of any other subject, one must assume that certain conditions will exist after the war. Postwar conditions as envisioned by the multitude of writers and speakers on the subject, run all the way from Utopia to chaos, and, of course, none of us knows whether it will be either of these extremes or somewhere in the middle. I suppose I am inherently a "middle of the roader" and for that reason shall string along with the weighted average and offer the following unoriginal prognosis.

(1) *There will first be a period of hesitancy, partially psychological, but more real due to contract termination, reconversion, and adjustment of industry from war to civilian production.* This will be particularly evident for six months to one year after cessation of hostilities in Europe. Obviously, for some it will be drastic and cover a much longer period; by others it will hardly be noticed, but as to its pronounced effect on the entire economy, six months to one year should suffice for this first period.

(2) *This first period of hesitancy will be followed by a period of general and perhaps great prosperity.* Originally this will be engendered and stimulated by the spending of tremendous wartime savings of individual consumers, covering their unsatisfied demands and wants created during several war years. Another early influence toward this condition will be the rehabilitation of war-wrecked countries with food, clothing, equipment and housing, in which, undoubtedly, we will participate by one means or another. Later, new industries stemming from inventions and scientific discoveries will undoubtedly appear. (I definitely do not agree with the mature economy theory.) Veterans' bonuses and benefits will be added to these other stimuli.

This period of high activity in both consumer and capital goods should last from five to ten years. During this time, there will be definite danger of rapidly increased inflation. However, like Babson, I believe that we have had gradual inflation for forty years or more and this is not to be particularly feared if we can control its growth.

(3) *This second period of prosperity can be continued indefinitely or it can be followed by deflation and perhaps collapse.* Lest you be unduly alarmed by this last pessimistic possibility, I should like to state here that my discussion today will end just before we arrive at that dismal point in the future.

With respect to the nature of accounting in the first postwar phase of termination, reconversion and adjustment, I shall devote little time. The problems presented are so imminent, so urgent and so intricate that each of them deserves far too much study and consideration for today's session. Termination of war contracts is already with us. The problem of preparation, presentation and collection of claims and disposal of surplus inventories is unquestionably the first and most important problem of industrial accountants at the moment. The problem of unscrambling government and private properties is here now and will be with us for several years to come. The conservation and provision of funds for transition purposes require our utmost efforts. But all of these primary postwar problems are receiving, and will continue to receive, concentrated thought and attention by all of us through other and more specific media.

It is to the nature of industrial accounting in the second postwar phase that I wish to direct more attention today. This is the longer period of prosperity which I have blithely predicted and which I wishfully like to consider as a normal condition for industry in this country. Furthermore, I firmly believe that it is within the power of America to enjoy a fair degree of continuing and even increasing prosperity with comparatively minor fluctuations. In the realization of such a future, the industrial accountant can and must occupy a vital role.

In my mind, a planned economy, collectivism, statism, or any other "ism," can neither produce nor retain the standard of living enjoyed in the past by this country. Even less can it hope to improve that standard. You cannot increase the size of the pile by subtracting from the top and adding to the bottom. Perhaps some good is served by placing a floor under the bottom, but there is only one way to increase the pile and that is by adding to the whole. The system that produced the fastest and greatest economic growth in all history, together with the highest standard of living, can still go forward and continue to demonstrate its prewar accomplishments.

That system is the profit system. True, it has its faults and weaknesses. The millennium is not here nor will it arrive in our time. On the other hand, I certainly do not feel that the profit system deserved the kicking around which it has received from politicians and professional reformers during the last dozen years. But I do think business itself permitted conditions to arise that allowed these opportunists to abuse and destroy the faith of millions in a system of which these millions were the greatest participants and beneficiaries. As a result, the profit system has been reduced to such a low point in public opinion that we have had to coin new names for it, such as free enterprise and free opportunity. But to me it is still the profit system. It has worked well and it can continue to do so.

Boiled down to its simplest elements, the profit system is the exchange of goods or services by which the original owner receives more than his cost. Unfortunately, the public has been led to believe that it is something quite different. In the mind of the public the profit system is more closely related to speculation, monopoly, restraint of trade, unconscionable profits, unemployment, special privilege, and almost all of our other social and economic ills.

For that belief, business is partly, if not chiefly, responsible. Too often those conditions did exist in or originate from business. Perhaps in a small minority of cases but frequently enough to provide the ubiquitous agitator and reformer with a single brick upon which to build a monumental structure of indictment and accusation. If business had been more alert to stamp out any and all violations of what I like to call "good business practice," we would not today be trying to think up some new and fancy name to avoid the opprobrium connected with the name profit system. And in saying that business has been delinquent in keeping its own house in order, I include the industrial accountant as one of the responsible parts of management.

The nature of postwar accounting as applicable to the industrial accountant will be essentially the same as it *should* have been before the war. When I give you my opinion of the requirements and responsibilities of the postwar industrial accountant, you will hear only what everyone in this room has heard many times before. Although all of you have heard it before, and perhaps the great majority of you believed it and practiced it, the fact remains that in the past too many of us have all too frequently followed the course of expediency and, in so doing, contributed in our own small way to the near collapse of public faith in the profit system.

In using the term "industrial accountant" today, I mean "cost accountant" in the broadest sense of the term and am using the two expressions interchangeably. I think previous speakers today have demonstrated that we can safely leave the guardianship and application of the principles of general corporate accounting and auditing to the professional accountants and to the teachers of accounting. Although the principles of cost accounting are fairly well defined, the successful application of those principles is a tactical operation which must be performed at precisely the right moment on a dynamic and constantly changing industrial front. This does not mean that the cost accountant's value is based on action alone. Performance as the result of emotion or impulse has no place in the manual of cost accounting. All decisions and actions of the industrial accountant must be based on mature judgment and consideration, made possible by seasoned experience and by study of all material available, not only on the

subject of accounting but with respect to the entire economy of the industry involved.

But so long as the industrial accountant confines himself to recording financial history, he remains only a necessary evil in the eyes of management. When he begins to help make tomorrow's history with today's facts, he becomes a productive and vital part of management itself.

On the theory that all business is formed to make a profit by furnishing goods or services of a social or economic value, it follows that the cost accountant's duties as part of management are to assist in that function. Any of my ideas as to how he may best accomplish that task are neither new nor original. Howard Greer, who will speak to you this evening on another subject, covered the present one most ably in his address at the annual meeting of the American Institute of Accountants last fall, and he has repeated it several times since before other gatherings. Harry Howell, also, has written and made numerous talks on this same subject.

The most important responsibility of the industrial accountant is to control costs, *which means to reduce them*. May I repeat that. The most important responsibility of the industrial accountant is to control costs—*which means to reduce them*. A static cost is not controlled. American industry did not arrive at its present preeminence by "holding the line" on costs. To paraphrase one of my old high school mottoes, and in slightly stronger language, to stay where you are, you must run like hell. Under the profit system, if you do not reduce your costs, you are not running fast enough, but your competitor will, and, as the loser of the race, you will become just another business statistic. Ruthless? Yes, but socially and economically far better than bureaucracy ridden, nonprofit governmental enterprise, perpetuated by incompetent and irremovable parasitic managers and employees.

Cost reduction will present a tremendous and fertile field in postwar days. We frequently hear the remark that cost accounting has more or less collapsed during the war, or has at least come dangerously close to it. I do not think that is exactly what has happened. In this connection, I am reminded of an old story but one which I think is quite appropriate under the circumstances. A small farmer sold a supposedly sound mule to another of his type. The next day the purchaser returned the animal and told the seller that the mule was blind. The seller denied this and after some warm and lengthy argument, the buyer said he would prove his contention. He led the mule out into the barnyard, pointed him toward the blank side of the barn, gave him a sound slap and told him to get up. The mule obliged and continued straight ahead until he crashed into the side of

the barn, whereupon the purchaser turned to the seller and said "You see, I told you he was blind." The seller scratched his head a moment and then said, "Naw, that mule ain't blind, he just don't give a damn."

Now, I think that is what has happened to cost accounting during this war. Neither the public, labor, management nor government seems to give a damn for the time being. Labor and the government are opposed to high profits; management and government are against high wages; and labor, management and the public all three dislike high taxes; but none of them seems particularly concerned about high costs.

The public seems reconciled to the fact that wars are costly, and, with the tremendous increase in national income, it has been generally able to carry its increased tax load without much sacrifice. Labor is realizing its stated long range aim of getting a larger portion of the national income and does not seem to realize that, in the same long range, it will pay a larger portion of these high costs. (Or will it?) Management seems to be more concerned in publicizing the natural and expected reduction of astronomical starting-load costs than in worrying about bringing present costs down somewhere near to where we know they should be. The government makes its usual good political gesture of eliminating corporate profits through taxation and renegotiation, passing over the fact that both of these encourage high costs through removal of the profit incentive.

I should like to state here that I am in favor, for the time being, both of high taxes and of renegotiation; they are both justified. But the fact still remains that they are part of the many forces engendering and encouraging high costs. There are many other such forces inherent and, perhaps, unavoidable under present circumstances: A seller's market, emphasis upon production above everything else, politics, selfishness and greed, to name some of them. But, regardless of the causes, we definitely have today a general attitude of "to hell with the cost," which will stand out in the days to come as our most serious economic aftermath of the war. Which brings us back again to the nature of postwar industrial accounting.

As I stressed earlier, the most important responsibility of the industrial accountant as part of management is to reduce costs. This was true before the war, during the war, and will be true after the war. The only way we can retain the profit system after the war is to produce and distribute more than ever before and at a lower cost. And for the record, I am not suggesting that this should be done by deflating basic commodity prices and hourly earnings. Obviously, the industrial accountant cannot accept the entire responsibility for the successful accomplishment of this task. Capital, labor, technology, government, and management other than the accountant

must all share this responsibility. But it is not our concern today to tell these others how to do their job. We have a big one already laid out for ourselves.

Now how shall the cost accountant best discharge that responsibility? What tools can he use? Again, I have nothing original to offer. The tools are not new, although some new ones may well be designed. Budgets, standards, incentives, inventory control, all have proven their worth. But more important than all these is a generous amount of good old fashioned horse sense (sometimes called psychology) mixed with initiative, aggressiveness and imagination. If budgets will produce the best results, by all means stress budgets—straight line or flexible. If the head of your company does not believe in standard costs, give him actual, differential, job order or process, but give him what he needs to reduce his costs and selling prices. If inventories are important, use lifo, perpetual or periodic physical, but use the one that best does the job. If labor or management will improve under incentives, design something that will best bring out that improvement. Cost reductions cannot be laid down in textbooks as precise formulae. They are the combined product of knowledge, experience and vision applied under rapidly changing conditions, but their attainment is not impossible. It has been done in the past and it must be done in the future.

Perhaps you are beginning to wonder when I am going to get down to cases and start talking about some of the specific details and procedures of postwar industrial accounting. Perhaps you expected a comparison of actual *vs* standard costs, or basic *vs* current. Maybe you are interested in departmental overheads as compared with machine rates. Or you might like to hear something of the relative value of last in, first out as opposed to first in, first out. Depreciation is always a fertile field for discussion. We might even resurrect interest on investment.

If you expected a detailed discussion of the relative merits of these today, you will be disappointed. All of these subjects have many points of interest and value, and in normal times should be given careful and thoughtful consideration. But these are not normal times. Details of procedures as compared to the necessity of cost reduction itself are relatively unimportant. Business and industry are definitely on trial. The war has demonstrated industry's tremendous productive capacity in an unlimited seller's market. If it cannot justify itself in the postwar competitive market, there will be no need to discuss the fine points and techniques of industrial accounting for the profit system, for free enterprise, or for free opportunity. There won't be any.

CHAIRMAN LOHNES: Thank you very much, Mr. Monroe. I think you will agree with me that our two speakers this afternoon have certainly covered this subject, however not so well but what there must be some questions in your minds, so while they are still on the platform here is your opportunity. So let's have some questions or some discussion on this subject.

MR. CLARENCE C. BROWN (Fisher Aircraft Division, Cleveland): I will ask these questions of Mr. Monroe. Logan says the cost accountant is at fault for some of the criticism that has been directed toward management. He also says that the position of the cost accountant will remain fundamentally the same after the war. I would like to ask Logan whether or not he thinks there is a good field here for more independence—-independent thought and judgment on the part of the industrial accountant, such as Mr. Stempf suggests, that is enjoyed by the public accountant.

MR. MONROE: Right at the start you may remember I told you the industrial accountant had no inhibitions in talking before a group like this, but I made the side remark "unless his boss happened to be in the audience." My boss isn't here today, so I cut loose.

Certainly, the industrial accountant cannot be as independent as the professional or public accountant. I do not recommend that. As a matter of fact, I am not criticizing the industrial accountant's lack of independence so much as I am the fact that through the 25 or 30 years that I have tried to absorb a little cost accounting, I have been bored to tears by hearing speaker after speaker get up and argue the merits of departmental overhead versus machine rates, or straight-line versus accelerated or any other of the numerous ways of writing off depreciation. Those things are important, but I still contend that the cost accountant's job is primarily to assist industry and management to reduce cost, and the point I am trying to get across to you all is that, in the great majority of cases, the industrial accountant has confined himself to discussing the theories and principles of accounting, and I claim we can get all the help we need in that respect from the professional accountants and the teachers of accounting. Let the industrial accountant devote his effort to reducing cost which will not only help the economy as a whole but will show pretty good results in his own bank account.

I don't know whether I answered your question, Mr. Brown.

MR. BROWN: Well, you have, Logan. I think I can agree with your thought there, except that in my experience as a cost accountant and many years of association with cost accountants their philosophy in accounting seems to follow the same line of thinking as the head of the company. In some cases, it is rather liberal and in some cases it is rather reactionary, but most of the accountants I know reflect the same philosophy as the head of their particular company.

On the question of reduction of cost, I think there is something else to be said. I think there is plenty of evidence that costs have been reduced. The cost accountants have been on the job during the war. We know of a manufacturer of airplane starters and gyroscopes in Cleveland, who claims he has reduced the cost many times from what it was before the war.

We have heard recently about one airplane manufacturer who, on a new order that has been taken, has reduced the cost per airplane by \$130,000. I think there is plenty of evidence that points in this direction. Carman Blough has

referred to it in some of his discussions in connection with defending renegotiation, that there is plenty of evidence that costs have been reduced during the war.

MR. MONROE: I would like to rebut that a moment. I do not say that costs have not been reduced, in fact, I said management is publicizing the reduction in costs, but if there is in this room an industrial accountant who thinks his costs are where they should be, he and I have a radical difference of opinion. Costs everywhere today are excessive, including the Cleveland manufacturer of airplane starters and gyroscopes.

I still say that costs can be reduced further and further, but probably will not be reduced much under the wartime economy, but when we return to a civilian economy we are going to have to reduce costs or we will have another '29 and '30 problem not five years from now but within two or three.

MR. PALMER W. HANCOCK (Owen-Illinois Glass Company, Toledo): I would like to ask Mr. Monroe a question. Don't you think that one of the jobs of the industrial cost accountant, in the near future, is a re-examination of the probable normal volume, the normal capacity to be expected? That is, everyone is practically operating on full maximum capacity now, but after the war the normal capacity of many businesses will be different from what it was during the war period. That may involve the matter of excess capacity, but there may be a possibility of utilizing some of that capacity increase during the war, and that will then affect volume, it will affect costs, and, in many instances, will and should affect selling prices. What are your comments on that, Mr. Monroe?

MR. MONROE: Well, your question comes dangerously close to what so many of the postwar planners are saying. I have read a tremendous mass of postwar literature, and, honestly, the more you read and the more you listen to it, the more confused you become. At times I am quite pessimistic about any long-range planning, and I think the time to establish the norm is now. I do not say don't plan and think about the future, but, as I said somewhere in my paper, the industrial accountant's job is more of a tactical job as a line officer rather than a staff officer. He does not plan strategy so much as he executes tactics. That, at least, is my impression of industrial accounting. Perhaps my own idea is wrong. The more I think about planning for the future on the long range, the more confused I become.

Frankly, I believe in standards. I believe in establishing a normal. We have used standard costs in our company for 20 years, but, today, standards that are normal are tomorrow abnormal. That has been proven throughout industrial history.

I remember, back in the twenties, hearing Mr. Stevenson, at that time president of the National Association of Cost Accountants, propound the theory, very ably, that you are never to take business at or below normal cost. Well, even in those days I differed with him because there is no such thing as normal cost for tomorrow.

As Mr. Lohnes has said, I have been in the automotive parts industry for a long time. For the last 20 years I have seen our company, time and time again, take business lower than the cost estimated and in three or four months we were making a nice profit on it.

I am afraid of normals for the long range. Our whole economy and our

whole industrial history has been too dynamic I think for anything like a fixed or long-range normal. So my answer to you is rather indefinite, also rather negative.

CHAIRMAN LOHNES: May we have some further discussion on this subject?

MR. MAX M. MONROE (Inland Manufacturing Division, General Motors Corporation, Dayton): My question has to do with the increase in manufacturing costs as a result of the lack of control and of other factors which have come into our economy during the war. I have heard estimates varying anywhere from 10 to 25 per cent as to the increase in the cost from prewar years of the same articles made by the same processes due to the lower efficiency of workers, breakdown of machinery in the plants and increases in material costs. I do know from my own experience that estimates on postwar building costs are just about double what they were in prewar. Do you have any figures on that?

MR. MONROE: No, there were some figures given out at a meeting in Detroit recently of the automotive industry, where it was estimated, but not by anyone from Ford, that the postwar Ford would cost \$1,400, I believe. The selling price would be \$1,400 against around \$900, or 50 per cent increase.

Recently, I attended a meeting of manufacturing executives, all top executives, and the question was asked and a poll taken, as to the relative efficiency of their labor, war and prewar, and the answers ranged from 50 per cent to 85 per cent compared with prewar efficiency. They were all, however, in the automotive industry, which is supposed to be high pressure and perhaps their opinions might be a little biased.

On material costs, I wouldn't care to offer any opinion. I do believe our material costs as such have been pretty well controlled, and I am not opposed to wartime controls such as that. I think we need them and we may need them for a while after the war, but there is no law or regulation that prevents any man, be he laborer or executive, from doing more work than he is doing now.

CHAIRMAN LOHNES: Do we all agree that all of our cost increases are due to inefficiencies or intended inefficiencies? Do we realize that in this period we have had to train new employees, and that we have lost many of our old, experienced employees, in addition, possibly, to a change of attitude? Isn't it possible that following this period, as a result of having learned many things regarding methods, new facilities, new tools and possibly substitute materials, and after having gone through another training period when again we will have to train men workers to take the places of women workers who will retire to their homes and when we can take advantage of those situations that we will again, even with higher labor rates, through more efficiency and the use of necessary facilities, be able to supply our products to the public at reasonable prices?

I hesitate to think that an automobile which sold at \$900 prewar is going to sell for \$1,400 postwar, because to my mind just that sort of thing is the thing that is going to bring about further pressure from labor groups to increase labor cost and then again if labor costs increase, the old never-ending cycle will start and that is the thing that brought about the inflation in Germany following the previous war.

That to my mind is one of the most dangerous things that we have to face, and it is only through this effort on the part of, and I am not going to put all the responsibility on industrial accountants—I expect a little bit of this effort

to come on the part of public accountants also, I mean C.P.A.—I don't think your effort is going to be confined to stating whether or not the assets are there. I don't think your responsibility is going to end with stating the financial position of a company at the end of a certain year. I think you have a greater responsibility to the public and your clients than that. I do not say many of you have not already assumed that responsibility, but I think you have it just the same as the industrial accountant, and we have all got to work to one end, and that one end is to better cost control and at the same time control prices and through that we will be able to control our profit way of life.

THIRD SESSION

FRIDAY, MAY 19, 1944—7:00 P. M.

Deshler-Wallick Hotel (Dinner)

Chairman:

WALTER C. WEIDLER, *Dean, College of Commerce and Administration,
The Ohio State University, Columbus*

Address: "Private Enterprise in a Planned Economy"

HOWARD C. GREER, C.P.A., *Vice President and General Manager, Kingan
and Company, Indianapolis*

INTRODUCTORY REMARKS

By WALTER C. WEIDLER

*Dean, The College of Commerce and Administration, The Ohio State University
And Others*

CHAIRMAN WEIDLER: Ladies and Gentlemen: I face this audience with mixed emotions. I am happy to see so many old friends again. As one gets older, I suppose he gets a bit sentimental about old friends. I know I do, so it is a very real and genuine pleasure to see so many faces here of people who have been with us through six conferences and are here with us for the Seventh Accounting Conference.

I am happy to see some new faces, because the new faces mean an opportunity to extend our friendships. We hope you newcomers will enjoy and profit by the conference. If so, we hope you will come back and see us again and then in the years to come we can greet you as old friends.

I am happy because tonight we have, at least in the City of Columbus, three of the four faculty members from the Department of Accounting who are on military leave. I refer to Professors Taylor, Miller and Fleig. Of course, it is a very real pleasure to us at the home stand to have these men from military service return for this meeting.

I said my emotions were mixed. They are indeed, because there is a saddening side to the picture. We meet again in the shadow of a great war. One tries to find encouragement where one may, and I think we do find encouragement that the accounting profession is meeting here in the shadow of this great war, in an attempt, in the American spirit, to solve the problems which present themselves, and to lay plans for the future. I am glad to see that.

I am saddened that from this assembly of friendly faces one face, in particular, is missing. I refer to the ruddy face and keen eye of your friend and my friend, Dr. Stuart McLeod. Doc was with us in six of these conferences, and we knew him as a highly versatile and accomplished personality. We knew him as a man who had made a great contribution in the development of that great association, the N.A.C.A. We knew him as a wise counselor. We knew him as a great wit. We knew him as an incomparable story teller. We knew him as a great friend. I am sure Doc in a very real sense is with us in spirit tonight, and I am sure he will be with us in spirit through what we hope may be many of these conferences in the years to come.

Now I have said that I was especially happy because we had with us on this occasion some of our own faculty who are in the military service and who have returned for the evening. To my right is Professor Jacob Taylor, Chairman of our Department of Accounting and now a major in the army. As I look over the audience, I don't see Captain Hermann Miller, also one of our professors of Accounting, on leave of absence for service with the navy, but here or not, we are all very proud of Captain Hermann Miller, and we wish him a speedy return to the campus and to the Department of Accounting. We also have with us this evening one of our instructors in accounting, who is a lieutenant in the army, Lieutenant Fleig. The fourth member of the Department staff in military service is Mr. James R. McCoy, who unfortunately cannot be with us.

Now a man who has put a lot into this conference in planning and administration is Professor Russell Willcox. I want to thank him for his services in the development of this enterprise this year.

(Dean Weidler introduced the following guests at the speakers' table.)

MR. CARL F. STEEB, Business Manager, The Ohio State University.

MR. BLAND L. STRADLEY, Vice President, The Ohio State University.

MR. VICTOR H. STEMPE, President, The American Institute of Accountants.

MR. T. J. DOLAN, President, The Ohio Society of Certified Public Accountants.

MR. H. J. SCHELLENGER, Director, Bureau of Public Relations, The Ohio State University.

MR. GRANT R. LOHNES, Past President, The National Association of Cost Accountants.

The next gentleman is very well known to all of you, and, again, he is one of the old-timers to this conference. Mr. William F. Marsh, the past president of the National Association of Cost Accountants. Won't you say a few words to us, Mr. Marsh?

MR. WILLIAM F. MARSH (Lybrand, Ross Brothers, and Montgomery, Pittsburgh, Pa.): Dean Weidler, Honored Guests, Ladies and Gentlemen: First, may I express my appreciation for the invitation again to be with you tonight. I have attended most of the Accounting Institutes of Ohio State and each one of them have I enjoyed.

About a month ago, Russ Willcox wrote to me and said that there was a possibility that Jack DeVitt, the President of the National Association of Cost Accountants might not be able to be with us during this conference because his boy is being graduated this week-end, I believe. He is getting his wings as a pilot, and that is a very, very good reason I think for Jack to be absent, and I agreed to substitute for him at the afternoon session. Unfortunately, I didn't have a priority and I was chased off an

airplane and my good friend Grant Lohnes, at the end of the table, presided for me, and I arrived here this evening about seven o'clock, and they asked me to say a few words tonight on behalf of the National Association of Cost Accountants.

This evening I have the feeling, for some reason or other, that I am occupying a chair that I do not desire. I think I might be occupying a chair for a moment of Dr. McLeod. In that capacity I feel very humble and very incapable.

To those of you who knew Dr. McLeod, even slightly, as Dean Weidler has said, he is with us tonight in spirit even though he has gone. During the past quarter of a century, Dr. McLeod, through his leadership, his personality, has built up an organization of approximately 15,000 people interested in accounting. But more important, it seems to me, again inspired by that leadership, interested and with the fixed determination shall I say to make men and women who want to come and enjoy their friends. That, ladies and gentlemen, it seems to me that man has accomplished. He has built a monument, as I see it, for a man whom we all love.

Doc always came to these conferences. He loved them. Each one of them he planned to attend far in advance, just the same as he planned for the conventions of his national association, and he felt somehow or other that you at Ohio State had formulated a unique plan for educational development of accounting, and with that I agree.

I have enjoyed each one of them, and it seems to me that I could do nothing better tonight than to repeat an observation he made after one of the meetings here several years ago, in which he said that you of Ohio State didn't need to thank the National Association of Accountants for participating in these conferences, that we of the National Association were grateful to you for the invitation to attend. I wish to add, also, we do thank you for the opportunity to participate in these institutes. Thanks.

CHAIRMAN WEIDLER: Thank you, Mr. Marsh.

There is another gentleman with us tonight who has been with us many times in these conferences, Mr. John L. Carey, secretary of the American Institute of Accountants. Mr. Carey, would you care to say a word?

MR. JOHN L. CAREY: Dean Weidler, Ladies and Gentlemen: It seems a little trite, but I must say that I wish to thank publicly those responsible for giving me the privilege of being here in this Seventh Annual Institute on Accounting, which is one of the outstanding accounting meetings in my recollection. I say that in all sincerity, and my pleasure at being here would be complete if it were not clouded by the same absence to which others have referred, my friend Doc.

I have been given the job of bringing a message from the American Institute of Accountants, and the ordinary wordy type of message does not seem to me to be very appropriate. It seems to me perhaps more suitable, in view of what occurred this morning and this afternoon and what we shall hear this evening and tomorrow, about the problems that are confronting the accounting profession, and the industrial accountant, and the teacher of accounting in the immediate future if I told you what the National Association of Certified Public Accountants is going to try to do about these things.

First, let me say that the Institute has grown in a very short time, about six years, from small business to at least moderate size business; from 5,000 members to 8,000; from a circulation for its magazine of 11,000 to 22,000; and from an income of about \$130,000 to nearly \$275,000.

About two weeks ago the Executive Committee approved a plan for a staff organization. It is a broad plan. It won't be put into effect immediately, but it is the announced objective of the Institute in the near future, and it illustrates, perhaps, as quickly and as well as anything could, the scope of the job that the Institute will try to do.

It is planned to have a director of research in addition to the regular administrative staff through which all the committees will function. It is planned that the director of research will have three full-time assistants, one dealing with accounting, one with auditing, and one with taxes.

In addition, a new post is called for, a director of education, and his job will be to coordinate the work and be responsible for all the staff work done with regard to the educational activities of the Institute, which include the work on the standard examinations which are now used in about 46 states and territories for C. P. A. examinations; the project that was mentioned this morning on selection of personnel, which includes the problem of aptitude tests; the project of postwar refresher courses for returning accountants who have served in the armed forces, which is under consideration; the problem of student societies or staff training, which was initiated just before the war; cooperation with the American Accounting Association; and the education problem at the university level, and similar activities.

Then, there will be continued the director of public information, whose job is indicated by the title; a new state society service department, the work of which will be to serve as a source of information for all state societies, a central agency which can suggest programs of activity to the state organizations and, as far as it is possible, be a kind of secretariat for all the societies of certified public accountants.

Then there will be continued the library and bureau of technical

ormation, the editorial department, the legal counsel, who is also our
islative advisor. With this staff organization and the committee structure
ich will be above it, it seems, at present, that the Institute will be able to
l continuously and effectively, we hope, with any problems in which
National Organization may take a legitimate interest. Thank you again
the privilege of being here.

CHAIRMAN WEIDLER: Thank you, Mr. Carey.

We are honored this evening by having with us the Honorable Frank
rlson, member of the Congress from the State of Kansas, who under-
nds the language of this group. I am going to ask Mr. Carlson to speak
ord at this time.

HON. FRANK CARLSON: Dean Weidler and Friends of Ohio, and
rounding states: I assure you it is a pleasure to meet with this excellent
up this evening.

I thought the Dean was going to say that I understood taxes. For-
ately, he didn't. He said understood some of the problems of this group.

It is a real pleasure just to meet with groups of this type and I, per-
ally, am glad to be here and I think I can speak for the members of the
ays and Means Committee and for Congress, and say that we are pleased
see these gatherings.

You can imagine my surprise when my good friends Vic Stempf and
in Carey came to Washington and suggested, as accountants and as the
sident and secretary of the American Institute of Accountants, that we
plify taxes. Imagine that! That really happened.

It was my pleasure to meet at a dinner meeting with the Executive
mmittee of the American Institute of Accountants two weeks ago in
w York City. I do not know how many were present, probably 100,
l I went back to Washington and told my colleagues that I had been
attendance at meetings of quite prominent industrialists but that the
cutive group of the American Institute of Accountants were more
sperous looking than the industrialists.

Now we in Congress need your help and that is the reason I am so
ased to come out here. I did not come out here to impart wisdom; I
ne out here to get an infusion of some of the methods and some of the
as that you can give to me that I can bring back to Congress. When
see groups like this gathering and in all seriousness and earnestness to go
o the problems which are facing this country now, and will be even more
icult in the postwar period, then I think there is some hope for this
ntry.

You know we got in a depression a few years ago. We like to forget
ut it, but at that time we had to gather around and figure out what to

do next. I don't know if there are any farmers here or any bankers, if so, you may not appreciate this story. This particular farmer shipped his cattle. His returns came back from Kansas City and as we farmers do, we sit around after supper—not dinner—it is the evening meal, and kind of think what we have done in the past day or past week, and this farmer's cattle returns were bad. He sat and figured on those returns and he found they lacked \$2,000 of taking up the note at the bank. He went to bed but he couldn't sleep. He got up and walked the floor a while, tried to go to bed again. He just couldn't sleep. Finally, at one o'clock in the morning he called his banker and said, "Mr. Banker, I have my cattle returns today. They just lack \$2,000 of taking up the note at your bank. It just worries me, so I can't sleep."

The banker said, "Mr. Farmer, you go back to bed. I will sit up the rest of the night."

Now this type of group had better be assembling in every section of the nation. I mean it is time that we begin to get our house in order, and I am not going to talk about it this evening. I am going to talk taxes tomorrow.

I just want to throw out a few thoughts and I want to leave this with you, that the history of every backward nation is characterized by oppressive taxation that sooner or later consumes so much of the productive capacity of that nation that it destroys it, and we this year are collecting 38 per cent of the national income in taxes, as compared with 5 per cent in 1900, 14 per cent in 1920, and the only reason we can do it is because we are engaged in a terrible war that tests the patriotism of all of us. But we must make some changes if we are going to continue this country as a democracy, continue it with the heritage that our forefathers left us. That is the thought I want to leave with you, and tomorrow we will continue and discuss Section 722 and carry forward and carry back some more things. Thank you.

CHAIRMAN WEIDLER: Thank you, Mr. Congressman.

A few years ago a man by the name of Dr. Harvey Davis was appointed to the Vice-Presidency of The Ohio State University. I have been a member of that faculty for over 30 years and I have never known an appointment to meet with more general approval than the appointment of Dr. Davis to our Vice-Presidency. It is a very real pleasure to me to present him at this time. Dr. Davis.

DR. HARVEY DAVIS: Speaking for the University administration, at the moment I need only say that it is very gratifying to see this group of accountants come back to the campus each year to this meeting that our College of Commerce and Department of Accountancy arranges. When

the freshmen come to a class, it is not great flattery to the teacher, because if they do not get there, the word goes around to the Dean and something happens about it. Even when seniors do not come, there is still a threat that they might not graduate, but when you people come it is purely because you want to come, and because you think there is something here that is worth having. Consequently, the University is uniquely gratified and uniquely pleased that you find year after year our program here attractive enough to bring you back in spite of difficulties of transportation, in spite of the overload of work that you have, and in spite of general problems that are surrounding you.

So I say again we welcome you very heartily to the campus, though you are not at the moment on it, but a good many of you were there today, and we are gratified to have you here.

CHAIRMAN WEIDLER: Thank you, Dr. Davis.

A long, long while ago I had the privilege, as a student in Harvard University, of sitting in the classes of the very great Professor Taussig, Professor of Economics. I remember that when Professor Taussig wanted to speak in terms of the very highest praise of someone's intellectual attainments, he spoke of him as a man of keen, incisive judgment, and that phrase "keen, incisive judgment" registered rather deeply with me. I thought about it a good bit, and I thought about individuals in connection with it.

It was a long, long time ago that I put just that label on Mr. Howard Greer, who is our next speaker. I had the privilege of associating with him as a colleague on the Ohio State University campus. He was one of us, and some of you may remember that he was at one time Chairman of the Accounting Department, and then he went away, we thought and hoped just temporarily. He went to the Institute of American Meat Packers and he was to be gone a year, and then that stretched out into two years, and then, to our very great regret, he thought it necessary to leave us and stay with the Institute. Then, subsequently, he went to Kingan and Company, of Indianapolis, meat packers, of which organization he is now the Executive Vice-President.

I don't mind saying that tucked away in the back of my mind there is still a lingering hope that sometime Howard Greer will return to the fold, and again invade the College of Commerce at Ohio State University.

I think most of you know of Mr. Greer. As I said, he has now for a good many years been battling with the problems of administration, and he is going to talk this evening on the subject, "Private Enterprise in a Planned Economy." I mean it from the bottom of my heart when I say I am very proud and very happy to present Mr. Greer to this audience.

PRIVATE ENTERPRISE IN A PLANNED ECONOMY

By HOWARD C. GREER, C.P.A.

Vice-President and General Manager, Kingan and Company, Indianapolis

Most programs now being suggested to promote America's future well-being involve a large measure of government planning and control. The public is assured that the private enterprise system will be preserved, but with its faults and failings eliminated through the watchful supervision of a beneficent and omniscient government.

Can this be accomplished? Can private enterprise continue, in a planned economy, to pour out the stream of benefits to the general public which have made this nation the richest and most powerful on earth? This question is worth studying. It is not at all certain that in a planned economy private enterprise will survive. In fact, it is not at all certain that under such conditions even democracy will survive. In other nations it has not.

If we want both private enterprise and planned economy, we should be thinking seriously about what is essential to preserve them both. Basically, the two ideals are in direct conflict. To reconcile them will require a high degree of statesmanship, from both enterprisers and political leaders.

The problem is to understand thoroughly the functions of private enterprise, to express precisely the objectives of planned economy, and to harmonize these two opposed methods of reaching our goal. We should recognize that the adjustment will be perplexing and painful, and that its accomplishment will cause both headaches and heartaches among people in all walks of life. It is not a task to be undertaken lightly, or with the assumption that success will be quick and easy.

Consider first these two contrasting mechanisms for satisfying public wants, as we know them. Private enterprise, practically unaided, served the needs of this country for the first three hundred years of its recorded history. Its benefits are apparent, if not appreciated. The way in which it functions is well understood by a good many people, including some members of college faculties. It needs neither eulogy nor explanation in this gathering. Planned economy is something relatively new. Our experience with it in this country dates back not much more than twenty-five years. Only in the last fifteen years have we had any considerable experience with it. Its

faults and merits are only beginning to make themselves evident to the public at large.

We can, however, already observe certain fundamental defects in our present economic planning and its administration. These defects are obvious to any who have been compelled to conduct private enterprise under the system of government controls in operation during the past few years. It may be worth while to catalog some of these fundamental defects now, as a preliminary to an attempt to cure them. If we fail to cure them, we must either abandon planned economy altogether, or else abandon private enterprise, and probably democracy along with it. The latter alternative has been experienced by most other nations.

It is not necessary to consider the effectiveness of our present planned economy as an adjunct of carrying on war. The features with which we are concerned are those related to peacetime occupations. The way in which wartime controls are being exercised gives a fair indication of the way peacetime controls are likely to operate.

Much present wartime control, as a matter of fact, has nothing to do with raising or equipping armies but is concerned with regimenting civilian life to promote supposed national welfare. Its objectives include controlling inflation, stabilizing wages, rationing commodities, stimulating production, regulating the exchange value of commodities, and maintaining public morale. The pattern of these activities may be expected to persist after the war, unless we take drastic action to change it.

There is one thing about which we should make no mistake. Any planned economy involves regimentation of the lives and activities of all citizens. It already has been demonstrated that we cannot have controls in general without having controls in particular. For example, if you start out to change the character of our food supply, or the amounts available to various classes of citizens, you inevitably wind up by telling every farmer what he can produce, and every consumer what he can eat. There isn't any middle ground. It is futile and dangerous to start on a control program unless you are prepared to go all the way.

This does not bother the economic planners. They feel that everyone will be better off when an all-wise government directs the details of his daily living, than when he is allowed to choose freely how he will occupy himself, and what he will do with the fruits of his labors. We have passed from the era when businessmen said, "The public be damned," to the era when planners say, "The public is too damned dumb to understand."

As applied to civilian occupations and enjoyments in peacetime, our present planned economy discloses certain basic deficiencies. These include

lack of accepted basic principles, competent administrative personnel, efficient and economical mechanisms, public support through voluntary law-observance, freedom from short-sighted political pressure, and measures of effective performance. Each of these deserves some consideration.

Principles

The most obvious thing about our present planned economy is its complete lack of any fundamental principles. No one apparently has even tried to say just what the plans and the planners are attempting to accomplish, except in terms so broad and general as to be meaningless in specific application.

Many of the processes of adjustment (as to earnings, spendings, and satisfactions), which occur constantly in a free economy, are being interfered with and distorted by government controls, but without any clear statement of the objectives sought. Consider a few illustrations:

(1) *The relative income position of various social groups is being adjusted artificially, to create a supposedly more "equitable" distribution of national income.* What constitutes "equity" in this respect? Is it related to what you produce, or what you need, or what you want? What a man could earn once depended solely on what his fellows would pay him for the service he performed. Now it is controlled by what some governmental agency thinks is "enough." By what standard can "enough" be measured? Cases recently decided indicate that there is no standard except what seems expedient to the political powers at the moment.

(2) *Commodities are rationed, on the assurance that in a period of scarcity this will give everyone a "fair share."* What constitutes "fairness" in sharing commodities like meat, whiskey, shoes, and gasoline? Does it have anything to do with what you produce? Is it affected by your previous consumption of these products? Is it related to your age or occupation? If you use less of one item, should you receive more of another? Is the right to your share one that you can sell or exchange? After two years of rationing, there is no agreement on these points.

(3) *Controls involve the interests of both producers and consumers.* Which should be paramount? Should we grant the producer a chance to operate in the way to which he is accustomed, making the consumer accept the output and foot the bill? Or should we let the consumer select what he wants and pay what he can afford, and force the producer to live on the proceeds? In trying to answer this question, we should remember that the most important producers are industrial workers and farmers. Their means of livelihood is vital to them. What level of agricultural prices should we maintain to encourage marginal farmers? How much wages should the

public pay for the services of those who cannot or will not turn out a decent day's work?

(4) *The direction of business affairs has been a responsibility of the managers of business enterprises.* Now it is suggested that "workers" should have a part in management. How much should a manual worker have to say about the way a business is run? Should his vote be controlling on questions of what constitute reasonable working hours, or a fair day's output, or the authority of a foreman, or how often there should be a holiday? In other words, should the business be run to suit the wishes of its employees, or to serve its customers and its owners? Those who profess expertness in this field say that all these factors should be "considered," but they do not indicate what the results of the consideration should be.

Under the system of freedom of enterprise, these questions all answer themselves. People get what they earn, and pay what they think things are worth. If they are unhappy about their lot, they must take their own measures to better it, either individually or collectively.

If these simple principles are to be discarded, others must be developed to take their place. It will not be practical or tolerable to have a planned economy operating without any plan. The dangers of leaving directions of affairs in the hands of inexperienced autocrats, operating on the basis of personal prejudices, without any criteria to guide them, must be obvious from recent experience.

With no conscious direction of the thinking on these essential points, we run the risk of finding embodied in our philosophy such extraordinary principles as the following, all of which have had some acceptance in recent periods:

(1) For all citizens, a fair share is an equal share for everyone, regardless of wants, needs, or deserts.

(2) Rationing should be used, not merely to prevent inflation and assure orderly marketing of commodities, but to redistribute purchasing power among the population.

(3) In a controversy with a group of employees, the management is always wrong.

(4) The administrator of an Act of Congress has authority superior to that of Congress itself, and may dispossess, fine, or imprison citizens, without challenge of the legality of his actions.

It is doubtful whether anyone could win a national election with these as planks in his platform, but despite all public sentiment, they are on the way to becoming the accepted principles of planned economy, if present tendencies are permitted to continue. Others equally objectionable will find

their place in the structure, unless a sincere and energetic effort is made to provide a firmer groundwork for this new system of affairs, which is to assure the next generation of richness, happiness, and indolence.

Personnel

The major difficulty with planned economy as it has been operating is the complete lack of trained, competent, and experienced personnel. The machine will not run properly until someone learns how to run it. Up to now, no one has learned how. This is no criticism of present-day administrators—merely an observation of their lack of preparation for their jobs. It is painfully apparent to anyone who has contact with government bureaucracy, including a good many of the bureaucrats themselves. You cannot have had experience with something that has never happened before.

Present-day administrators have been drawn largely from two groups, both of which have displayed a conspicuous ineptitude for the tasks assigned. This plainly is more the fault of the tasks than of the performers, but it gives some indication of the difficulties to be overcome in providing this new and complicated machinery with capable operators.

The first tendency of the government in the war emergency was to enlist businessmen as administrators, and to invest them with the responsibility for the proper functioning of whole industries under more or less rigid controls. They were supposed to know how business operates under ordinary conditions, and from this it was presumed that they would know how it could be made to operate under artificial conditions. Unfortunately, most of them didn't. The average businessman has an outlook limited by the circumstances of his own particular enterprise and the requirements of his own particular job. He is too busy to be a deep thinker on broad economic problems. He concentrates on his own affairs rather than those of the industry as a whole. In particular, he does not do much worrying about the troubles of his competitors, letting them do their own worrying.

With the problems of a whole industry dumped in his lap, with a demand that he keep prices down, wages up, production at a maximum, employment at a minimum, profits low, income tax contributions high, and everybody satisfied, he has found himself completely at a loss. When he has prescribed a regulation that looked as though it ought to work, he has found it full of loopholes for the unscrupulous, and unsuspected injuries to members of the trade he never knew existed. He usually has found, in no time at all, that he has made himself unpopular with everybody and has accomplished very little.

The second group on which the government has drawn is the college professors—economists, engineers, accountants, lawyers, and others. These

people, whose life has been spent principally in studying, thinking, and teaching, supposedly should be able at least to grasp the problems and develop the broad outlines of a solution. Unfortunately, their record as administrators is even less inspiring than that of the businessmen. Most of them started on their jobs with a complete lack of practical business experience, which means that they had no real knowledge of how the world of business actually operates. Worse, many made no attempt to learn, but put all their energies into trying to make business fit their patterns, instead of making their patterns fit business.

What the average professor-administrator does not know, and does not want to acknowledge, is that the operation of business enterprise is about 20 per cent economics and about 80 per cent psychology. People act part of the time like economic entities, but most of the time like human beings. If you are going to run a business, or an industry, or a whole economy, you have to recognize that. You must keep remembering that in America people will not do just what they are told, unless you make it easier and more satisfying for them to do that than to do anything else. If the regulations issued for their guidance are too long, they will not read them; if they are too complicated, they will not understand them; and if they are too annoying, they will not obey them.

Most members of business organizations act largely on the basis of ingrained habit. They do not rationalize their actions; they do what experience has taught them they can safely do without getting into too much trouble. Their powers of adaptation are limited. All this the professors have pretty much ignored. After years in the classroom, where no one disobeyed or talked back, they have come to suppose that all they have to do is to read a lecture and issue an assignment, and that ends the matter. In business, it doesn't.

Among my acquaintances in the bureaucracies, the businessmen have one point of advantage over the professors—they usually recognize their limitations and are anxious to learn. The same, unfortunately, cannot be said of many of the administrators from the academic world.

If neither of these two large groups offers well-equipped candidates for managing a planned economy, then from what source are they to be drawn? Plainly, there is none at the present time. One of the big tasks in making a planned economy work will be the selection and training of individuals to administer the program.

Mechanisms

The private enterprise system functions through literally millions of independent units, adjusted to each other in a set of complex and delicate

relationships. These have been worked out through centuries of trial and error and accumulating experience.

The problem of each unit is to adjust itself to those it touches, on a basis which permits it to be self-sustaining and productive. What it makes, what it consumes, and how it exchanges goods and services with others in the system are matters of constant, semi-automatic adjustment, which keep the system as a whole functioning with a reasonable degree of smoothness.

Sometimes the machinery creaks and clatters, and occasionally it threatens to break down altogether. In this country, however, there is no record of production and distribution ever coming to a standstill, or of any considerable group of individuals failing to satisfy their minimum subsistence needs.

One of the greatest merits of the system is one of its least obvious features, namely that it makes its own adjustments, and carries its own cost of operation. Each piece of machinery pays its own way, or ceases to exist. There is little or no costly "overhead" required to keep it functioning.

In this respect, a planned economy—even one functioning efficiently—is plainly inferior. It has to be constructed and operated by artificial means. It must develop elaborate mechanisms for accomplishing its objectives. It must hire people to make its decisions effective, and must pay them to do the work. This is a difficult and costly undertaking. Consider, for example, the problem of getting the nation's food distributed to 130 million consumers. Assume that economic planning calls for dividing the food among consumers, not according to their wants and their ability to pay, but according to some pre-arranged plan. How is this to be accomplished?

Under normal conditions, the distribution of food is accomplished almost entirely through the mechanism of varying prices. The people who want luxury goods offer enough in the market to get them produced. Low-cost staples move in bulk, at low handling expense, to consumers everywhere. A shortage of anything in one locality raises prices until more goods move in to satisfy the demand. A surplus lowers prices until the excess is diverted elsewhere. No one pays any taxes to get this job done. The costs are borne by the participants in the exchanges, and not by the taxpayers. The mechanisms already exist, and new ones provide themselves almost automatically when there is a need for them.

Contrast this with the problem of getting foods distributed under rationing. A complete new mechanism, of almost incomprehensible scope and elaboration, had to be created to do the job. Although existing agencies were used to a maximum degree, the Federal government alone had to add

tens of thousands of individuals to its staff, and to enlist the services of hundreds of thousands of volunteer workers. Industry assumed a staggering additional burden in extra personnel, extra procedures, and extra work for regular employees, tasks at which everyone probably would have rebelled at any time except during a war.

The operation of a planned economy involves an arrangement of this sort of mechanisms for practically every phase of production and distribution. They are all extra, that is, they are a net addition to the mechanisms already existing under a private-enterprise system. If there is duplication, presumably it will have to be eliminated by discontinuing some of the functions and pursuits of private enterprise. How long it will continue to be private enterprise under such conditions is problematical.

Law Observance

Law enforcement in America depends largely on the attitude of the public toward the laws. The tradition is one of voluntary compliance with laws of conduct which almost everyone accepts as fair and reasonable. This goes back to the earliest history of this nation. Authority exists by virtue of the "consent of the governed." Laws have been observed by the people because they have been made by the people.

The establishment of a planned economy calls for an entirely new kind of law-making. In place of statutes prescribing standards of equity for citizens in dealing with each other, we have now a multitude of detailed regulations of every aspect of economic activity. Instead of law-making by a legislative body, we have law-making by appointed administrators, who are neither chosen by nor responsible to the electorate.

With this change in the character of laws and law-making has come a complete change in the attitude of the public toward the laws and the law enforcement agencies. Instead of considering laws as a protection and a benefit, the average citizen now regards the great majority of them as a nuisance and an infringement on his fundamental rights. An economic structure built on that sort of public attitude is unlikely to be stable or successful. If half the citizens treat a regulation with contemptuous disregard, or are in open revolt against it, its enforcement becomes impossible. The task of the law enforcement agencies in such circumstances is plainly beyond their capacity. It is trite to refer to the federal prohibition law as the first and worst example of the actions which have tended to destroy conscientious voluntary law observance in this country. The NRA added another unhappy chapter to the history of attempted control of human relations by administrators and regulations.

Today, we have thousands upon thousands of similar regulations, many of which are openly disdained by large sections of the public. The flourishing black markets in many commodities are evidence of the impossibility of enforcing a program of planned economy without better understanding and support from the public than are evident now, even under wartime conditions. What the situation would be if similar controls were attempted in peacetime can be left to the imagination.

Political Pressures

The basic theory of a planned economy is that affairs will be organized and ordered according to a scientific long-range program, worked out by experts, to reach certain desired objectives. The proposal is to substitute for the haphazard, unpredictable course of economic relationships a carefully adjusted scheme of investment, employment, production, distribution, and pricing. This scheme is supposed to insure that everyone is kept busy, that we produce what we need and distribute it where it is wanted, and that wages and prices are in such adjustment that everyone has a chance to make a satisfactory living.

It is obvious to every thoughtful person that a program of this kind must be worked out with the greatest of care and foresight for a considerable time in advance, by men with the best available training and experience. Since the program will be intricate in the extreme, and the adjustments of the most delicate kind, it is plain that, once set in motion, the plan cannot be subject to constant tinkering, tampering, and interference, without producing a worse result than if there had been no plan at all.

It is characteristic of our democracy that anyone who does not like the way it is functioning may bring to bear such political pressure as he can command to get things changed. Large groups of persons are organized into political blocks of various kinds for this definite purpose. Political leaders are extremely sensitive to the activities of such blocks, and to the public demands of the important molders of public opinion, such as editorial and feature writers, cartoonists, and radio commentators.

If these two conditions are set down alongside, the violent contradiction between them becomes immediately apparent. The operation of a planned economy assumes, first of all, reasonable freedom of the planners from interference in carrying out complex, long-range programs. The functioning of a democracy insures a maximum of interference from political blocks, and other group interests, with anything the government may undertake which touches their special interests.

In our democracy it is generally true that men of predominant influence in the government will be politicians first and social theorists

afterwards. It is difficult to imagine them subordinating political exigencies to a theoretical plan for long-range economic betterment. When there is an election to be won, or a group to be mollified, the most carefully developed plans will be scrapped on a moment's notice. That this now happens every day in Washington is a matter of common knowledge. So far no one has found a way to insulate administrative agencies from the pressures of influential groups or individuals. Trade groups, labor groups, consumer groups, and just plain busybodies keep up a constant bombardment of demands and complaints, seeking special privileges, or relief from real or imagined hardships. When the delegations are headed by persons of known influence in the ruling political party, or by constituents of a member of Congress whose vote on the next appropriation bill is important, they simply cannot be ignored. Concessions must be made to satisfy the most vociferous and plausible of the demands.

With all these political pressures coming to bear, the maintenance of a sensible, comprehensive, well-integrated program becomes a superhuman task. The planner's original program becomes so twisted and patched that it cannot possibly function as intended. By the time some higher-up decides impulsively to junk the whole thing, to stop a threatened denunciation from a dissatisfied labor organizer or farm-group leader, even its own author will hardly mourn its passing.

The frightful muddle into which many of our home-front activities have fallen during this wartime period is due largely to this aspect of the American way of life. Plans may have been poor, and their administrators poorer, but none of them could be expected to function in the midst of never-ending interference from political-pressure groups and from the higher-ups in the government itself.

It is a question whether this handicap can be overcome in a nation devoted to freedom and democracy. Those who are honest about it will admit a doubt as to whether planned economy and democracy can both exist in this or any other country. There is an inherent conflict between them which cannot be overcome until the public and its politicians recognize a planning program as something which must be divorced from political pressures if it is to have any chance of success.

Economic Justification

The foregoing sections have mentioned certain defects in the planned economy with which we have had experience in the past few years. These are defects already obvious. There is at least one other, perhaps not quite so obvious, but inherent as a potential defect in any planned economy program.

This is the uncertainty of obtaining a fair test of the economic justification of any part of the program. There is a constant and serious risk of maintaining activities and enterprises which would not independently justify themselves through separate public support, but which may be embodied in the program through ignorance, prejudice, inertia, or political pressure.

The free enterprise system, as almost everyone realizes, has the advantage (from the standpoint of the general public) of ridding itself of unwanted and unneeded activities. Products no longer in demand cease to be manufactured. Services for which no one will pay are no longer rendered. An inefficient enterprise fails to survive.

Planned economy sets up new criteria as to the worthwhileness of various economic activities. If an administrator, or his political superior, decides that an activity is meritorious, he may force its inclusion in the overall program, whether the public wants it there or not. The customers lose their right to say directly what they do and do not want from business, agriculture, and labor. The administrator, in his infinite wisdom, decides the question for them.

Most administrators think their decisions are sounder than those of the public they serve. This may be questioned, even as a matter of definition. The fatal difficulty, however, is that the administrator is much more likely to be influenced by those who want to perform a service than by those who want it performed for them. The whole history of regulatory procedure is that it tends to be influenced far more by producers as such than by consumers as such. Producers organize themselves into compact, effective groups, and persuade government leaders that their needs are paramount. Producers, of course, include laborers and farmers, two of the most important political groups.

It is inevitable that in economic planning attention will tend to become concentrated on the vested interests of producers. People organize themselves quickly and actively to protect their means of making a living. They are much more positive and cohesive in their attitude toward their position as earners than as consumers. Nobody ever votes himself out of a job.

The danger of all of this is that the productive activity of the country eventually may be organized to perpetuate established ways of making a living, instead of to provide the greatest satisfaction of human wants. Group interest, rather than the broad public interest, is likely to be most influential with economic planners, or those whose political power gives them the opportunity to do the planning.

The tremendous impact of war demands has suppressed, temporarily,

the civilian demands of the producer groups, at least to some extent. We already have, however, plenty of examples of regulations designed solely to protect the existence of various classes of enterprises for which there is no present need or demand. This would almost certainly be the pattern of regulation in peacetime.

Fallacies

Without rejecting the idea that planned economy is inevitable, it is worth while noting that arguments for it often involve certain contentions which are strictly fallacious. Some of these certainly should be eliminated in measuring the probable advantages of this way of organizing our economic life.

Experience with what measure of planned economy we have already had indicates that no dependence can be placed on some of the common assumptions as to what such a system would accomplish under peacetime conditions. The following, for example, are almost certainly unwarranted:

(1) *That controls will be exercised for the benefit of the public at large, rather than to improve the position of individual groups.* All the evidence indicates that planning certainly will be done largely in the interest of certain groups. People wishing to appraise its probable effects on their own lives should be concerned chiefly with whether they belong to a group, or can organize or join a group, which will profit by the advancement of its interests relative to those of other groups, through artificial changes in the operation of natural economic laws.

(2) *That operation of our economy under a system of overall planning is more flexible and adaptable than under a system of free enterprise.* It has been claimed that persons in touch with all aspects of the economy, and with authority to make arbitrary adjustments as seemingly required, will be able to stabilize production and distribution, and avoid the causes of unemployment, shortages, surpluses, and fluctuating prices. Evidence accumulated to date indicates that fluctuations in our economic position have never been so wide, so erratic, and so utterly unpredictable as since the economic planners suspended the operation of ordinary economic laws.

(3) *That private enterprise and individual freedom can survive a long period of rigid government control, extended to every feature of producing and exchanging goods and services, making a living, and enjoying the fruits of productive effort.* It is apparent already that private enterprises will cease to function effectively if every aspect of their operations is to be regulated in such detail that their executives have time for nothing except attempts to comply with or combat government regulations. It must be evident, also, that the individual citizen likewise will lose not only his

economic freedom but also even his political freedom if he becomes permanently subject to the dictates of a planned economy. His right to redress in the courts for infringements of his liberties already has been drastically curtailed. His right to ask his congressman to help him influence an administrative agency soon will have to be sacrificed also, if the whole scheme of economic planning is not to be wrecked on the rocks of political interference.

Essentials for Success

Most thoughtful people who believe in economic planning will agree that the program is not likely to be successful or satisfying if we try to administer it without basic principles, without trained personnel, without adequate and economical mechanisms, without voluntary public cooperation, without freedom from political interference, and without objective standards for measuring its contributions to our national welfare.

It would seem that those most interested in the program would do well to undertake the formulation of the necessary philosophical and administrative foundation on which a program can rest securely. It seems necessary that we have a "plan for economic planning," if we are to have any chance of doing the job effectively.

Consider the parallel of the position of the thirteen colonies, when, freed from English control, they found it necessary to prescribe a set of principles and working rules to govern their new nation. They assembled the best minds and wrote a constitution. Our modernists consider it a very archaic document now. Some of them ought to get together and write a better one to govern our brave new world.

Plainly, it would have to prescribe some means for overcoming the weaknesses already apparent in our first experiments in setting up a planned economy for America. How could this be accomplished?

I am not a candidate for a seat in this new constitutional convention, but I can suggest a few of the things which will be necessary to make economic planning successful:

(1) *Establishment of an "Economic Policy Board—a nonpolitical, nonpartisan group of "career" statesmen to develop the general principles of public policy which should guide national economic planning.* This board should draft recommendations of the broadest character, indicating how and to what ends productive activity should be directed. It is conceivable that such recommendations might be adopted as planks in a party platform, or might serve as the basis of pledges by political candidates, as to the kind of economic planning and control which would be attempted by the administration they seek to constitute.

(2) *Establishment of a program of education for economic planning.*

This would consist of training, in higher educational institutions, of individuals seeking a career in this field. If it is assumed that private enterprise is to continue as part of a planned economy, the preliminary education of these administrators should be supplemented by a liberal apprenticeship in business. The qualification for eventual appointment to an administrative position would be a satisfactory scholastic record plus a satisfactory rating by a sponsor in the business world as to efficiency and dependability in human relations.

(3) *Creation of an administrative organization, modeled on business lines, with suitable assignment of authorities and responsibilities, and provision for coherence and continuity in policy and operation.* General policies would be laid down by a "Board of Directors," appointed by the party in power, but with the understanding that the administrative organization would be wholly free from political interference in carrying out the details of the program. No business organization can function successfully on any other basis. No government organization in the field of business can hope to do so.

(4) *Development of specific measures of public service, to be applied to the government-planned program, in place of the "profit and solvency" test now automatically applied to private enterprise.* Some means must be found for letting the public pass, in some direct way, on the merits of the activities conducted under economic planning. This is necessary to avoid having the program cluttered up with an accumulation of obsolete and unnecessary activities. Means would have to be found for obtaining fair tests of public sentiment on such matters as quality and cost of goods and services, to replace the normal operation of the laws of demand and price.

Conclusion

All this envisions a conscious effort to frame broad public policies, and to implement them with effective procedures, to accomplish the idealistic social objectives claimed for most programs of economic planning. The conception of a pooling and submerging of individual selfish desires, in the interests of an overall program designed to aid everyone, is noble enough to warrant a demand for a broad, nonpartisan, unselfish approach to the problem. A test of the true idealism of many proponents of such plans may be found in their willingness to engage in such an undertaking.

The alternatives are worth consideration. If the trend toward economic planning is permitted to continue along its present line, it will be merely an encouragement to those with selfish interests to grasp, by political means, group advantages which their economic contributions do not war-

rant. Such a struggle would engender tremendous bitterness, and it is by no means certain that those groups expecting the greatest advantages would actually realize them.

It would mean that private enterprisers would have to transfer the bulk of their energies and efforts from productive accomplishment to obtaining greater political influence. The community might expect joint action by owners and workers in each industry to obtain preferential treatment. Advertising campaigns would be directed to voters instead of to consumers. There would be the utmost in effort to obtain the inside track with the economic planners, and to exert influence on the administrative agencies charged with carrying out the plans.

No one should suppose that this activity could be expected merely from the big bad wolf of big business, or that it would be reduced by the present political ineffectiveness of business as such. Every class in the community would become a potential seeker of preference from the economic planning administration. Existence would become impossible for any citizen who could not attach himself to a group with the necessary political influence to protect his particular position.

This tendency already is quite strong. Its damaging influence on progress and public welfare already is painfully apparent.

There is a danger that in such a struggle some of our most cherished institutions may be lost. This danger will grow to monstrous proportions, unless we do one of the two following things as soon as the war emergency has passed:

(1) Reduce government controls as quickly as possible, and restore a maximum of individual freedom and private enterprise in satisfying the nation's wants.

(2) Establish a program of economic planning based on idealistic principles, and conducted by men of statesmanlike attainments, who will devote themselves to public welfare, and not to the selfish interests of special groups.

Until public leaders are ready to meet this challenge, the future of private enterprise, and even of democracy, will remain in doubt.

CHAIRMAN WEIDLER: Thank you, Howard Greer. I think you will all agree with me when I say that we have had a keen, incisive talk.

FOURTH SESSION

SATURDAY, MAY 20, 1944—10:00 A. M.

Commerce Auditorium

Chairman:

JOHN C. MARTIN, *Keller, Kirschner, Martin and Clinger, Columbus*

Address: "The Future of Federal Taxation"

HONORABLE FRANK CARLSON, *United States Representative from Kansas,
Member of House Ways and Means Committee, Washington, D. C.*

Address: "Two Important Postwar Tax Problems That Should Be Dealt
With Now"

WALTER A. COOPER, C.P.A., *Peat, Marwick, Mitchell and Company,
New York*

INTRODUCTORY REMARKS

By RUSSELL S. WILLCOX
Accounting Department, The Ohio State University
and

By JOHN C. MARTIN
Keller, Kirschner, Martin and Clinger, Columbus, Ohio

MR. RUSSELL S. WILLCOX: Dean R. E. Glos of Miami University, who was to have presided this morning, is unable to be here, and Mr. John C. Martin, of Keller, Kirschner, Martin and Clinger, of Columbus, will preside. Mr. Martin.

CHAIRMAN MARTIN: We are about to begin our final session of this Seventh Annual Institute of Accounting. In my opinion, this is the climax and the most important session of the Institute.

Everyone of us is interested in taxes, most of us in two ways, both as taxpayers and as tax preparers.

We had a sample last night of the first speaker's information, and everyone was very much impressed with the few remarks that were made. One remark, particularly, impressed me, and that was that 38 per cent of our national income was being paid in taxes, and that that had gone far enough. One of my associates said, "Well, that is the first time I knew anybody in Washington was thinking along those lines, so maybe there is some hope."

We are particularly fortunate in having Mr. Carlson to discuss the topic of "The Future of Federal Taxation." Mr. Carlson is a member of the House Ways and Means Committee. He has been in Congress since 1934 representing the great State of Kansas. Without further remarks, I am glad to give you Mr. Carlson.

HON. FRANK CARLSON: Mr. Martin, Members of the Ohio Institute on Accounting, and Friends: It is a real pleasure to meet on this beautiful campus this morning. It is a relief to get out and away from the streets and buildings, and worse than that, the confusion in Washington, into the great open spaces, so I am very pleased to be here.

I want to mention that it is a privilege to serve with a distinguished citizen from this state on the Ways and Means Committee. He tells me he is a graduate of this University, Class of 1907. He is not only a man of

ability, but he is a man of high character, the type of man we need in Congress, and he is none other than Tom Jenkins. Ohio is fortunate to have that gentleman in the Congress of the United States.

I want to talk to you this morning about some very serious problems and I am going to follow a manuscript. I do not like to follow a text, but it will assure me of some sort of terminal facilities, and, also, I want to keep the discussion on Federal taxation.

THE FUTURE OF FEDERAL TAXATION

By HONORABLE FRANK CARLSON

*United States Representative from Kansas; Member of House Ways
and Means Committee*

I hope you will forgive a Kansas farmer and livestockman for presuming to come here and speak to you Ohioans about government. Your Buckeye state has produced seven Presidents, and manages to keep a contingent of senators and representatives of outstanding calibre in Washington.

It is my private opinion that I was asked here for an infusion of your higher learning; that you folks decided, after looking over the tax situation, to do something for the nation and quietly bring in someone from the Ways and Means Committee of the Congress for indoctrination in some of your own hardheaded, timeworn principles which make for progress and well-being. In all seriousness, I am honored by your invitation to come and speak to you. It is a most serious assignment. I wish I had the eloquence to inflame this whole nation to the vital importance to all of us, collectively and individually, of planning right now the tax program we shall require for peacetime happiness and prosperity.

Why is this so important?

Here's why: All those warm, delightful freedoms that we talk about and preach about—economic freedoms and personal freedoms—can be as completely destroyed by vicious and short-sighted tax policies as they would be by the rule of a conquering Tojo or Hitler. For instance, in our Federal tax structure we allow tax credits for gifts and contributions to churches, educational institutions and philanthropies. Now just suppose the Congress changed this sound policy. Suppose that tax laws made it practically impossible for our churches and other private institutions to exist. What then happens to our cherished freedom of worship?

Suppose we let some of our professional business baiters have their way about taxing private industry. Suppose rates which now range up to 95 per cent are carried over into the postwar period. How then could our business concerns make up the gap in our economic life which will come about when government spending drops from a war level of more than \$100 billion to an anticipated peacetime level of \$18 to \$20 billion? If we make it impossible for our factories, our farms and our stores to busy themselves in peacetime activities, what then happens to our freedom of opportunity and the jobholders' freedom from want?

The point is, with the war on its way to being won, this is no time to grow careless of our national economy. It has had a terrific shock, with taxes reaching toward the point of diminishing returns. But, after all, our American economy is one of the very things we are fighting for.

Our national policy in taxation, as well as in other matters, must clearly encourage our people to depend upon themselves first, and upon government second. I hold that government is the servant of the people, unless, as Thomas Jefferson said, we can find an angel in the form of a King. When government uses its power to levy and borrow in reckless manner, the pattern traced throughout all history is of government becoming the master of the people, and, inevitably, a decline in national strength with lowered standards of character and living. The great mass of people, ultimately, have suffered from unsound fiscal policies.

Look down the centuries—Jerusalem, Babylon, Athens, Rome. Old glories buried in rubble, empires broken down by tax loads, skeletons in history's closet that rattle in our ears. Today the rubble is piling up again in Rome, also in Germany. Let's look at their mileposts to infamy.

They began with bewildered, muddled statecraft, and a confused, desperate national economy. Comes the depression and a dictator who knows all, does all. The people barter freedom on a false altar of security. Then came juggled deficit financing, huge public works, big armies, bitterness between labor and capital. They called it "National Socialism." Inevitable social unrest must be blamed on something, so minorities are persecuted, and finally a nation sees an answer in the spoils of war.

More and more we hear discussions of a postwar world where peace is to be fostered by international harmony and economic stability. Yet these things must begin at home. International relationships never can be satisfactory unless internal conditions are sound. One of our greatest contributions to the future peace of the world can be to put our own financial house in order by establishing a national policy of wise government spending, a stable currency, balanced budgets and a positive program of debt retirement.

This is our traditional fiscal policy. With its help these United States grew fast and strong so that today the world almost takes for granted that we shall not only perform a modern miracle of war production, but that we shall be strong enough to underwrite the peace as well.

This year the Federal government has a budget of \$104 billion, mostly for war purposes. We will pay in only about \$45 billion of taxes. The difference is a big deficit, yes—but \$45 billion of taxes is more in volume and more per capita than any nation under the sun is paying or ever has paid.

\$104 billion going out; \$45 billion coming in. That is the way this year's books do NOT balance. We are just borrowing that balance. It can be called deficit financing, although plain people simply refer to it as "going in the red."

I do not have to tell you that we could not raise even close to \$104 billion by taxation. If we tried to raise that amount by taxes, our war effort and everything else would stop functioning. Taxes, even in wartime, reach a point of diminishing returns. In a way, it is good that they do, for it is a constant reminder that the precious things bringing us victory today—labor, enterprise, industry, and national muscle—grew on a land relatively free of taxes, and I do not think they will grow in any other soil.

Let's take a look at our rising tax thermometer. At the turn of the century, taxes were 5 per cent of the national income. Taxes were 14 per cent in 1920. In 1944, the economists predict that they will amount to 38 per cent of the national income. Only patriotism in time of war will tolerate such great diversion of income to government.

One of the most effective ways of improving the Treasury's position is to scrutinize carefully the expenditure side of the budget. Every dollar that can be saved means one less dollar of present or future taxes. I am afraid we have become too careless with hundreds of billions and other astronomical figures in recent years. Fifty million taxpayers are awakening to the fact that it is their money that is being so loosely tossed about.

So much for the immediate problem, which is only a small taste, only a beginning of the critical days ahead. In considering the postwar tax program, we are trying to determine what our needs will be, for it will be a tragic travesty on a glorious and costly victory if that program is not wisely planned and soon.

We shall come out of the war with a debt of \$300 billion. You have to put down some figure. That's the one I put down. The debt is not all for war; it is the accumulation of 14 years of deficit financing. We haven't had a balanced budget since 1930.

Now, if we pay 2 per cent interest on that \$300 billion debt, we shall have \$6 billion to pay in interest annually. Not many years ago, \$6 billion would have carried the whole government cost.

So we'll have interest on the debt, and we must try to write off the principal as we go along. If we should set aside as much as \$10 billion annually for debt and interest repayment, it would take three generations to get a clean slate.

Here are some other major items that will be saddled onto the nation's taxpaying power in the coming days of peace:

- (1) We are going to maintain a big army and navy.
- (2) We are committed, with our Allies, to help rehabilitate destitute nations.
- (3) We are committed to muster-out payments for our sons and daughters coming home from war.
- (4) We are committed to the hospitalization and rehabilitation of veterans and their dependents.
- (5) We have made extensive investments abroad in facilities of war and trade—South America, Canada, Egypt, and elsewhere—to maintain, or liquidate.

The cost of our postwar economy, including these major items, is variously estimated to be from \$18 to \$30 billion dollars annually. But this figure is not nearly so important as the figure it must derive from—our national income.

Today we are able to collect \$45 billion in taxes simply because our national income is around \$150 billion. Had we tried to collect \$45 billion in 1932, it would have been necessary to confiscate practically every cent of income.

Right here is the major point of everything I have to say. Government, with its tax policy, must be as eager to promote a constructive peace as it was a destructive war. The soundest maximum we can follow is the American device of low rates and high volume. This is the only way to avoid subterfuges of inflation or debt repudiation. It is the American way. No imported false economies here. And it will bring us the volume of tax revenue needed to pay our bill like free men: to thus preserve our savings, our insurance, our pensions, the buying power of our wages.

Suppose, for a moment, we just consider the opposite conception of taxation from our time-proved way. Suppose we say: Let's have high tax rates and low volume. What happens then? Why the American family car will become a share-croppers' mule and the missives will go back to the washboard and spinning wheel of her grandmother's day. The guy who holds the mortgage this time will be Uncle Sam and his crew of tax collectors. High rates and low volume is nothing more than government of the government, by the government, and for the government.

How do we pay off? I offer you a constructive program of six points:

- (1) *By stimulated civilian production, freed of governmental control.* Farms, factories, mills, utilities, trains, steamships, stores must earn money to pay taxes. They will not have income to tax if government continues directives, regulations, priorities and confiscatory taxes. Some controls, I

grant, are needed to hold back inflation and black markets, until production can more nearly meet the pent-up consumer demands at the close of the war. But production must be freed of restrictions at the earliest moment.

I like to think that tomorrow's peaceful world will hold tremendous opportunity. The opportunity system made our nation great. It can make it great again. And it can bring it nearer to a sound position more quickly than any other system which has sprung from the mind of man. Let's have no more of class legislation that stifles ideas for production and keeps idle the wealth that should be producing national income and making jobs.

(2) *Small companies and new enterprises should be spared at least a part of the tax responsibilities of established concerns until they achieve footing in the economic life.* The automobile, the radio, and the airplane all came out of small shops. Continued progress is inseparable from free enterprise of the individual, which of necessity starts from small beginnings.

The war has played havoc with small concerns. A Department of Commerce study showed that 273,000 firms, mostly small ones, went out of business from June, 1940, to June, 1942—an average of 450 each working day.

Small business not only brings vigorous growth to our economic life, it also has a profound social significance. The small businessman is an important part of our community existence. Many of our returning veterans will establish their own enterprises as a way of life as well as a means of earning a living. The independence and vigor of small companies shall be encouraged by definite tax concessions.

We Kansas farmers think we particularly have common cause with the small businessman. A livestockman is just as much in the meat business as your corner butcher or the meat packer. We stockmen are small businessmen. And that is why I know that all business, big and little, needs only the chance to prove that economic and national progress are one and the same thing.

(3) *Obstructions to the flow of capital into productive industry should be removed.* It is a healthy sign to hear so much discussion of eliminating all or part of the double taxation on corporate dividends. The working man has a great stake in this, for it takes about \$6,000 of plant, machinery and working capital to provide one person with a job. A wise tax structure will bring venture capital into productive, employment-giving enterprises.

I suggest we revise our tax structure so that individuals will be encouraged to put their savings to work in postwar America, as savings have been put to work in this nation since its beginning.

(4) *The pending tax bill, the so-called simplification bill, goes a long*

way toward wiping out taxpayer perplexities. But the tax law should be simplified even more. As you know, the simplification bill deals only with personal taxes—business taxes are still to be considered. The entire code on Federal corporate taxes must be scrutinized, and unproductive but bothersome tax levies eliminated. For instance, the declared value tax and the related capital stock tax, which actually produce only an extremely small net revenue, should be eliminated.

Please do not think I am here trying to inject personalities or politics, but I feel it my duty to tell you quite frankly that we Republicans anticipate having to carry the weight of the responsibility in meeting the coming historic fiscal crisis of staggering debt and postwar tax problems. That is the reason our minority leader, Representative Joseph Martin, has named a committee on taxation of which I am a member. We are preparing for the job. And I am particularly anxious concerning the future of the corporate income tax, for it is my special duty in this Republican group, as chairman of the corporate tax sub-committee, to formulate an incentive tax program. And if any of you boys can help a poor Kansas cattleman, I urge you to give me the benefit of your ideas.

Also, at the close of war we should terminate the excess profits tax. In this country and in foreign countries, the excess profits tax has been used primarily to capture war profits, but the very nature of the tax has made necessary various optional methods and innumerable relief provisions which have added reams of confusing technical provisions to our tax statutes. In dropping the excess profits tax when peace comes, we can simplify our tax law and regulations in very substantial degree.

(5) Hand in hand with simplification, our future tax policy must contemplate an improvement in the administration of the tax laws. We must encourage tax officials of the highest calibre and make it worthwhile for them to remain in public service and free them of domination by political forces.

The cost of tax compliance in the United States is tremendous. Business taxpayers, particularly, feel the impact of more than 175,000 tax collecting bodies. The Federal government is, of course, the number one tax collector, and the administration of the federal tax statutes involves billions of dollars of manpower and effort on the part of both taxpayers and government. I believe we have a serious responsibility in the Congress to examine the matter of tax administration and to write tax statutes which will foster certainty and equity.

The intent of Congress must be made so plain that there will be little chance of inequity or misinterpretation. As a matter of principle, the

executive branch of government should not be empowered to determine income, deductions and taxes within its own discretion, for it will be only a question of time that such powers will be used for political or punitive purposes.

(6) *Finally, when we have our house in order and our economy at work on a truly democratic basis, we must intelligently gauge our earning power, set our tax sights on the maximum business and trade and employment, and cut the cloth accordingly.*

I believe some economists hold that if taxes go beyond 25 per cent of the national income, they begin to reach a point of diminishing returns. That is to say, a 40 per cent rate might produce less money than a 20 per cent rate simply because business production and taxable incomes would begin falling off under such a tax load.

Well, we are now taxing the nation about 38 per cent of its national income. That is more than economic law allows. The only reason we get by with it is because Uncle Sam is underwriting practically every major industry and service. When he steps out of this responsibility and releases those controls, my friends, we must cut the tax rate.

If our national income after the war runs at a rate of about \$125 billion yearly, it is my belief that we would be foolhardy to attempt to levy more than \$10 billion in state and local taxes and about \$18 to \$20 billion in Federal taxes. If this is our postwar tax limit, we must keep the expenditure side of the budget within governmental income.

We would do well to remember that \$18 to \$20 billions of Federal government is a lot of government. We used to get along quite well in the 1920's, for instance, on one-sixth as much. There is no magic in large-scale spending by government. If it has any virtue at all, they lie within narrow and temporary limits.

I have a great faith in our future. I know there are those who look to government as the cornucopia from which all blessings flow. But that frame of mind is a foreign importation. When our young manhood returns from the four corners of the earth they will bring with them—and to us—a better appreciation of American standards of self-dependence in a framework of self-government.

Why, we have had some professors tell us that we would be better off with trillions instead of puny millions of debt. But, as a friend of mine says, those fellows have upside down brains. I'll venture they have a hard time running a farm or grocery store on that theory.

Our eternal hope, now as always, is the moral fibre of America. We spent hard dollars; we borrowed hard dollars; we will pay back hard

dollars. What's done cannot be undone—as Lady Macbeth said—and so with honest purpose, let us get on with the job of making our own future.

CHAIRMAN MARTIN: Thank you, Mr. Carlson. It has been very apparent in all of the papers and addresses which we have had during this meeting that the trend of thought in each is that some changes must be made. Mr. Paton yesterday and Mr. Greer last night indicated that considerable change must be made in order to continue our American way of life, but most of us are not able to do much about it. It is very inspiring to have Mr. Carlson, also, indicate that he knows the same problems which we have all recognized, since he is in a position to do something about it, and is doing something about it.

I had an experience recently in being privileged to serve on a special committee on taxation for the Ohio Chamber of Commerce, on which several very able tax attorneys of Ohio and several controllers and some practicing accountants met for the purpose of recommending, to the House Ways and Means Committee, simplification of the individual income tax return. This committee had several meetings last fall, but, unfortunately or fortunately, we were not privileged to have a member appear before the Ways and Means Committee, because they did not hold public hearings. However, when the Simplification Bill came out, in the framing of which Mr. Carlson and Mr. Tom Jenkins of Ohio had a very important part, we found every point in the bill which this committee could find to recommend. It was very encouraging to find that the Committee followed the thoughts of the practicing accountants along the lines of simplification. We can feel very much assured that our tax problems are in excellent hands with Mr. Carlson there, and we thank him again for this wonderful address.

We are going to change the program slightly. We had anticipated having a question period after our next speaker. However, since Mr. Carlson has to leave in about 25 minutes, in order to catch his plane, we will take a few minutes now in which you may ask questions, if Mr. Carlson will oblige, and I am sure someone has something to ask him.

MR. STANLEY HITTNER, (C.P.A., Cincinnati): I have been fishing around for a bit of information concerning the introduction of Section 129 into the 1943 Revenue Act. I haven't had a great deal of success, and it occurs to me that Mr. Carlson, a member of the House Ways and Means Committee, might possibly throw some light on it.

Briefly, Section 129 reads something like this: "If any person or persons or if any corporation acquires another corporation for the purpose of evading or avoiding the assessment of taxes by the acquiring of an allowance, a credit or deduction to the corporation enjoyed, that the commissioner has the authority to look through such acquisition and make such assessment as he thinks is fitting under the conditions."

As I understand Section 129, it is sort of an application of Section 45, which was in the previous Revenue Act.

Here is the question I would like to have some light on, Mr. Carlson. There are quite a number of small, closely-held corporations that are finding it an absolute necessity to dissolve and to operate in the partnership form. Their credits or excess profits taxes are so small that they find it practically imperative

in order to stay in business to dissolve their corporation and to reorganize as a partnership.

Now the point that has been raised is as to whether the persons who acquire the assets of that corporation may possibly find themselves in the position of having them assessed as a corporation after the partnership has been formed. Would you throw some light on that?

MR. CARLSON: That is one of those problems that it is hard to say how it will work out. This particular section, the amended section, has an interesting history. We were confronted in the Ways and Means Committee with this situation, and I think we might just as well speak frankly. Large numbers of advertisements were appearing in papers, an obsolete corporation with a capital stock of so-and-so many thousands or millions for sale at five cents on the dollar, to avoid taxes. Practically to that effect. We had copies of these advertisements in our committee. We discussed it seriously. We did not want to do anything that would in any way endanger a bona fide corporation in their corporate tax structure for tax purposes, but we thought we had to do something in order to protect the Federal government from folks who were trafficking in these corporations, and it was a most serious problem.

Now it may be that this is working to a very extreme hardship in a number of cases. If it is, I can assure you that the committee and the Congress will want to correct it, but we were confronted, as we often are, with some of these problems that are so difficult to handle.

If you folks have suggestions on that and changes that should be made, where bona fide corporations are being forced to discontinue, shift from partnerships into corporations or vice versa, let us know and we will see if we can't do something about it.

That is the history of that particular piece of legislation.

CHAIRMAN MARTIN: Any further discussion?

MR. WILLIAM GLYNN (Department of Taxation of Ohio, Columbus): Mr. Carlson mentioned that in a two-year period from June, 1940, to 1942, there were approximately 275,000 small businesses dissolved or forced out of business. He also mentioned that in our postwar income tax plans we should try to encourage new businesses, possibly by making concessions to new businesses in the way of income taxes. I have been wondering how we are going to sell some of our larger corporations and their shareholders on the idea of going easy on some of the small businesses who may, in five or ten years, be on an equal competitive basis.

MR. CARLSON: I knew I would get in trouble on that one. I am not at all surprised because that is a difficult problem, and, as I said at that time, it is not tax equality, but I believe we must do something to try to keep these small corporate businesses scattered over this nation. There is a tendency right now to pool everything in large groups, and to me it is not good for the future of this national economy. I just do not think it is. It would be nice now to have just one agency dealing in automobiles, one in airplanes, and one in something else, and these large businesses can and do manufacture and distribute their commodities at less than a large number of small concerns can do it, but I do not have automobiles and radios and those things in mind particularly. I had in mind small businesses—stores, partnerships and firms out in the cross-road country towns. I think we have to get them back and keep them there if we want to have

the kind of a country that I believe builds for a strong nation, and I think we are going to have to give some tax concessions to get those boys started, even with reduced tax rates, and I don't know what they should be. It has been suggested that we give them a tax credit in their corporate structure of \$3,000 or \$5,000 for two years, three years, one year. This doesn't mean forever. If they can start out without tax concessions, I would be the first one to be for it. I believe we have to study that.

MR. RALPH BALLINGER (Wilson, Finner and Company, Cleveland): I would like a little elaboration on this 38 per cent figure. Is that the overall? Is that the federal tax load, or over-all, or the Federal Income Tax load only?

MR. CARLSON: That is the present national tax load, which includes Federal and state taxes of \$45 to \$56 billion—about \$55 billion.

CHAIRMAN MARTIN: Are there any more questions? If not, we trust that many of you folks will take advantage of Mr. Carlson's offer to receive from you your suggestions about any tax problems, that is, the law-making side of tax problems. We can't ask him to try to solve our problems. We know there are two definite sides to taxation. One is the making of the laws and the other is the administration of those laws, and we are finding that they are sometimes handled in a rather divergent manner, such as Section 722, and our House Ways and Means Committee of Congress passed a relief provision, a provision in income tax laws to give relief to taxpayers but when we get into the administration of this tax law we find administrative authorities are a little bit more inclined to say, "Show me why you should have relief," than to offer relief.

I am sure Mr. Carlson is doing his job very efficiently. Thank you.

We will proceed with the next part of our program. We now have a man who looks at taxes more or less through the same pair of specs that we do, that is, through the operation and preparation of tax returns. Mr. Walter A. Cooper is a C.P.A. with Peat, Marwick, Mitchell and Company of New York. He has served as chairman of the Standing Committee on Taxation of the New York Society of Certified Public Accountants for many years, having been in practice for 27 years, and he is also a member of the Committee on Federal Taxation of the American Institute of Accountants. I am sure that he will have a good message and will be able to answer some questions after his talk. Mr. Cooper.

TWO IMPORTANT POSTWAR TAX PROBLEMS THAT SHOULD BE DEALT WITH NOW

By WALTER A. COOPER, C.P.A.

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I have two topics to talk to you about this morning. Both of them are sometimes referred to as postwar matters, and therein lies the rub, so far as I am concerned. I have in mind (1) the issuance of nonnecessity certificates, and (2) the current deduction of reserves for postwar expenditures attributable to wartime activities. It is my view that these are matters that should be taken care of now, before the arrival of the postwar period, or what might be more accurately referred to as the "postwar production period." We may very well have a substantial recession in our war production before the end of hostilities. This is starting to materialize to some extent through contract terminations (a very live subject in accounting circles these days), and it may well be that, like the rolling snowball, this situation will continue to grow, so that we shall have a gradual elimination of war production instead of the sudden cessation that was experienced at the end of the last war. At any rate, some companies are now experiencing many, if not all, of their postwar problems, and more are likely to face them in the immediate future.

Nonnecessity Certificates

One subject that is now giving some concern relates to the amortization adjustment that should result when emergency facilities cease to be useful in the interests of national defense within a period of less than five years from the date of acquisition.

As you are no doubt aware, Section 124 of the Internal Revenue Code provides that either as the result of a proclamation issued by the President declaring the ending of the emergency period, or as the result of the certification by the Secretary of War or the Secretary of the Navy that a particular emergency facility has ceased to be necessary in the interests of national defense, the amortization period may be shortened. This would not only give taxpayers who have been claiming amortization the right to restate the deduction over the shorter period, but would also permit those who have not been claiming such deduction to go back and claim it over

the shorter period, provided, of course, the facility has been covered by a certificate of necessity.

It is not to be expected that the President will declare the ending of the emergency under present conditions. However, there are a number of situations in which certain facilities have lost their usefulness, insofar as anyone can tell at this time.

The law provides that these certificates of nonnecessity may be issued by the Secretaries of the described Departments only in accordance with regulations prescribed by the President. Those regulations have not been issued, and, as a result, the expressed intention of Congress as set forth in the statute is being nullified because it is impossible, at present, for either Department to issue a nonnecessity certificate. Failure to issue these regulations is, I have been able to learn, not the result of an oversight or lack of time, but seems to be due to a lack of agreement between the Departments as to the need for the issuance of nonnecessity certificates. I understand that regulations have, in fact, been drafted, though not necessarily agreed upon by all parties, but that they have not been promulgated because there is a feeling in some quarters that the amortization provisions are too generous and should not be made more so by shortening the period through the issuance of nonnecessity certificates. Another argument that has been advanced in opposing the issuance of the necessary regulations is that comparatively few requests have been received for nonnecessity certificates, and, hence, that there is not enough interest in the problem to require action at this time. That, I think, is fallacious, because I have learned of a number of cases in which taxpayers have not asked for such certificates because they knew they could not be issued in the absence of the regulations, and they have been waiting the promulgation thereof.

My definite suggestion, therefore, is that all taxpayers who have facilities no longer being used because of changes in production under continuing contracts, completion of contracts without renewals, or termination of uncompleted contracts, should promptly file requests for the issuance of nonnecessity certificates. As the War Department has indicated the form and manner in which such application should be made, while the navy has not done so, it would seem desirable to follow the War Department's form in all cases. The filing of a number of such applications will indicate that there is a need for the issuance of the regulations, so that appropriate action can be taken to either grant or deny the nonnecessity certificate.

The inability to obtain these certificates has led some taxpayers, desiring not to hamper efforts to convert plants to civilian production, to

consider the advisability of physically scrapping facilities that are not being used, even though it would be quite possible to set them aside in condition to operate again if ever required. The Bureau of Internal Revenue has specifically ruled that if emergency facilities are permanently abandoned, loss may be taken without jeopardizing any amortization rights. However, if such facilities are not physically scrapped or disposed of, one is always faced with the problem of establishing the fact of permanent abandonment. Hence, the taking of such action as will prevent further use might be necessary to assure the taxpayer the right to deduct the loss.

We all recognize the difficulties of accurately determining the needs of our armed forces for war material. Mistakes were made in the past which have resulted in overproduction of some items. Perhaps, in the future, further production may be needed, even though that is not presently expected. Hence, our future war effort may suffer if facilities are scrapped and later further need therefor arises. It is natural that a taxpayer who has been subjected to top tax rates on income produced through the use of these facilities, but after allowing for only a partial deduction for the cost thereof, should seek to write off the balance at the same top tax rates when he sees no reasonable prospect for future use. Thus, a provision of the code carefully developed and, in fact, several times amended in an endeavor to benefit the war effort by removing taxation deterrents, may prove a boomerang if the intent of Congress is nullified by the lack of administrative action. Those of you who are interested in this subject should not only call the matter to the attention of your Congressional representatives, but also should move the matter along by filing applications for nonnecessity certificates.

Postwar Reserves

The second subject I want to discuss is postwar reserves, or, to state it more specifically, the current deduction of an allowance for losses, costs and expenditures that will be incurred after the end of the war production period and which will arise out of the circumstances existing during that period, the nondeduction of which will inflate the income reported for taxation during that same period.

I can say that it is a difficult subject to discuss, and even though some of us may talk about it fluently, it is difficult to handle legislatively and administratively. Like cancers and other ills with which we are all familiar, we do not like them and find them hard to take, but we must nevertheless deal with them. Also, if I may again use the cancer illustration, it is far better to treat with them before they become serious than after they become fatal.

We should all realize that virtually every business concern now working on war production or under wartime restrictions is building up a future expense that may be attributed directly to the present war conditions. They will be many and varied, and that goes for everyone—from the retailer carrying an inventory of substitute, inferior, or even “ersatz” goods to the manufacturer producing nothing but war material. The great majority of business concerns are today banking up one or more headaches for the future, that is, if they continue in business, and the last thing we want them to do is to go out of business. When I say “that is the last thing *we* want them to do,” I am including everybody. For those who are owners, the reason is obvious; for those who provide the labor and who might otherwise be unemployed, the reason is equally obvious; and the farmers need good business and employment to obtain fair prices for their crops. Others have only to consider their status under the existing heavy tax burdens with which they are encumbered. The extent to which that burden can be reduced in the future is necessarily predicated, on the one hand, upon the extent to which we can keep our labor employed and thus minimize government relief expenditures, and, on the other hand, upon the extent to which we can keep our business concerns productively active and paying taxes which would not be paid if they went out of business. Hence, the problem concerns everyone, whether they realize it or not.

Speaking in Columbus last fall, Mr. Randolph Paul, then General Counsel of the Treasury Department, had something to say about the idea of deducting postwar reserves, and, in the process, referred to the carry-backs of losses and unused credits as something that accomplishes the same result. I shall refer to that in more detail later on, but at this point I should like to say that I wondered, after I read his remarks, whether the Treasury was misleading Congress or Congress was misleading itself with respect to the government's fiscal picture. We have a law today requiring that each taxpayer pay a certain percentage of his income in the form of one tax or another based on net income. Our law says, also, that should certain contingencies develop in the future, that is to say, the realization of losses rather than income or the earning of less than the so-called normal income, some of the taxes previously paid shall be refunded. Those provisions were inserted in the law because it was recognized that such contingencies were certain to occur. I wonder, therefore, if Congress, in considering the revenue statistics which indicate that so and so many billions of dollars of revenue have been collected, has taken into account the fact that, under the law, some portion of that revenue must be refunded at a later date. True, they have not issued bonds of a type that we take into account in

considering our indebtedness, but, nevertheless, under the law of the land, the government is building up an obligation under its present laws to refund a portion of the tax that is being currently collected. Similarly, when the Treasury Department statisticians estimate the current revenue, the future revenue or the revenue under any projected change in the taxing structure, I doubt very much if they take into account the probability—in fact, one may say, the certainty—that some portion of the revenue currently being collected or expected to be collected will have to be refunded.

We accountants would never certify to statements that did not reflect potential future losses, even though estimated, as in the case of Reserves for Bad Debts. While government accounting is on a cash basis, there is no more real reason to disregard this future liability than there would be to regard bond sales collections as current revenue. A somewhat similar question arose when it was suggested that old age benefit taxes be treated as revenue, with results that are now well known.

As a matter of fact, some companies already have found themselves in position to claim refunds of taxes previously paid. While not serious at the moment, it could become a major factor in government finance if at some future date a sudden cessation of hostilities and of war production should result in a situation wherein many business taxpayers would not only pay no revenue to the government but would claim, and be entitled to, refunds of revenue previously paid and expended by the government.

To suggest that the carry-back provisions take care of the possible losses that may occur as a result of the accumulation of deferred costs or expenses arising out of the war effort is to recognize that the government has such an obligation. Yet, the proponents of the idea refuse to approve the issue of an appropriate paper or document to represent that obligation, and when it is not so represented it is too readily cancelled by a mere change in the law, as occurred in 1934 when the carry-forward of the net loss provision was stricken from the taxing statute. That could happen again.

Our government operates on the basis of receiving certain cash during the year either through revenue taxation or borrowing, which it uses to pay its expenses. It recognizes the bonds issued as being an obligation which must be paid off in the future. The similar, though inexactly determined or perhaps undetermined, obligation to refund some of the revenue because of subsequent losses or reduced income should be equally recognized. If the government does not so recognize it, can business count on it?

Hence, my proposal with respect to the current deduction of reserves for postwar expenditures resulting from wartime effort involves the issuance

of bonds that will currently recognize that obligation. It is true that it will not take care of all the circumstances or possible refunds, because some of them will result from postwar events not connected with war activity. Nevertheless, and regardless of that possibility, we do know that business is today building up a future expense that, in one way or the other, is directly attributable to the wartime activity. Let us recognize at least that much of our obligation.

Entirely aside from the question of government fiscal policy, other factors must be considered. It was suggested by Mr. Paul that carry-backs of losses and unused excess profits tax credits would adequately take care of those situations in which postwar costs properly attributable to wartime operations resulted in losses or reduced income; but as between taxpayers the effect of that provision may be most inequitable. In the first place, it must be assumed that all such costs or expenses will be incurred within the two-year, carry-back period, but there is no assurance of that in any given case. Secondly, such expenses or losses in the future may serve to reduce income otherwise taxable at rates lower than those prevailing during the war period. Of course, if it is contemplated that the present rates will continue for two or more years after the end of the war and that high tax rate income will continue until the war ends, that argument would be meaningless. But some of our legislators and some of our administrative leaders have intimated that the end of the war should be followed promptly by a reduction in the current high tax rate. Senator George, Chairman of the Senate Finance Committee, is one who has made such a statement and early this week a certain Republican Congressman expressed comparable views. Congressman Carlson has just confirmed this. Hence, it may be that a continuance of the present situation will produce a result in which those who lose the most in operations after the war will gain the most in tax benefits. That is putting a premium on inefficiency or wild spending.

It has been suggested, also, that because of the fact that the amounts of such deductions will not be determinable until after the end of the war, it is better to wait and see what happens, and one illustration used was the matter of paying dismissal wages to employees who may have to be dismissed when the current level of operations declines. Then, if it becomes necessary to pay dismissal wages, the prior year tax liability can be reopened and readjusted to allow such deductions. I leave it to you who have worked at taxes to say how much the Treasury Department will allow, under existing law, as a deduction in the year 1943, for example, for dismissal wages that are paid in 1945. The answer—nothing! Though the “wait and see” policy has been suggested, it has never been proposed that the law

be amended to reopen a war period return to allow a deduction for postwar expenditures for which the taxpayer did not become legally liable and did not undertake to pay until after the postwar period began.

The second feature that is important in this problem is that of the availability of cash to carry on the postwar reconversion or to take care of the expenses therein involved. One cannot replace an "ersatz" inventory, or convert plants, as examples, so as to continue uninterruptedly in business, without the required funds. In this connection, much has been said about the substantial increase in the amount of cash, government bonds, and other liquid assets of corporate business as tending to indicate that the corporate business financial position is becoming increasingly more liquid, in so far as the availability of assets of that type is concerned. However, there has been no attempt to compare the increase in corporate assets of that type with the corresponding increase in the liability of such businesses to pay Federal income taxes.

We all know that the government takes, ultimately, a very substantial part of the profits of business under existing conditions. However, it does not collect that until the following year. Hence, at the end of the tax year during which the income has been earned, it is quite natural that there should be on hand a very substantial amount of the most liquid assets of business. The operators who fail to recognize that fact and do not have the liquid assets available are very likely to find themselves in trouble.

I have not attempted to compile statistics for the country as a whole, but I do know from the figures of our own clients that, in many cases, the increase in such liquid assets has been less than the increase in current liabilities, including taxes. In some cases, the net current position or ratio has declined; in many others, where there has been an improvement in the net current position, I find that much of the improvement, or perhaps more than the net improvement, is in the form of inventory, which may or may not be liquid when the war ends.

Finally, it has been proposed that when it is anticipated that losses or unused credits will result in refunds, the taxpayer could be placed in position to defer the payment of taxes currently payable. That necessarily assumes that such anticipation will arise before the March 15 payment is due, and even then the potential cash saving will be limited to the previous year's liability. In many cases, however, it will be the latter part of the year when it becomes reasonably certain that such a result will come to pass. Certainly, that is now true so far as 1944 is concerned, and if taxes have already been paid, how can one defer their payment? If the last war should be a guide and the current war should end in November, we are very apt

to find that for the year in which the war ends little or no tax will be due, as the war end will certainly destroy or reduce values of many assets. Then potential refunds may well exceed the last quarterly installment that would remain to be paid. Hence, the cash that may be necessary to provide the liquid position to carry on with postwar expenses or reconversion costs would be severely limited, and reliance would have to be placed on obtaining a cash refund of taxes previously paid. Before that happens, the patient may be dead, because, after all, one cannot pay dismissal wages, extra unemployment insurance, replace inventories or what-not without the wherewithal, or proceed very far on the assumption that, at some date in the future, a tax refund will become available. We all know that many things happen between the filing of a refund claim and the receipt of the amount claimed.

Thus, some who oppose any plan to permit the current deduction of postwar reserves recognize the soundness and equity of the principle by suggesting the "wait and see" plan. Those of us who have sought refunds might add, "Try and get it." To provide cash, the deferment of taxes owing is suggested, with no assurance that the amount will be in any way adequate. However, the suggestion recognizes the need for providing the necessary funds; otherwise, not even abatement of taxes owing should be permitted.

I have proposed, and continue to urge, a definite plan for the allowance of a current deduction for estimated postwar expenditures, sometimes referred to as a deduction for postwar reserves, but with proper restrictions to prevent abuse of the privilege, and at the same time prevent the cash involved therein from entering into channels that might contribute to our inflation difficulties, and yet be sure that the cash will be available for the required purposes when the need therefor arises. It may be summed up in these six cardinal features:

- (1) Deductions should be elective to the taxpayer, to be taken by the taxpayer if he sees fit.
- (2) It should not exceed a certain specified percentage of net income, that is to say, excess profits net income or normal tax net income if the excess profits tax brackets should not be reached, of, say, 15 per cent.
- (3) The entire fund should be required to be invested in suitable, low-interest, or even noninterest-bearing government bonds which would become payable on demand within a very short time after the end of hostilities, say, 60 days, or other such reasonable period as may be required by the Treasury Department to arrange the necessary financing, and thereafter bear normal interest.

- (4) The fund should be expended within a period of three years after the end of the war.
- (5) It should be expended for any one of a number of specified postwar requirements or purposes.
- (6) If it is not so expended, the unexpended portion should be subject to tax recapture by the Treasury by taxing it at the rate in effect when the fund was created.

Let me enlarge on those six points and explain them a bit.

Deductions Should be Elective—Taxpayers desiring to place themselves in a sound position to carry on after the war should be permitted to take the deduction. However, as the plan suggested for allowing the deduction calls for compliance with other rules, no taxpayer should be required to take all or any part of the maximum deduction.

The Deduction Should be Limited—It is quite difficult, if not impossible, to estimate the amount that will be ultimately required for postwar purposes, reconversion and deferred costs. Some companies have made careful studies of their needs, but the best study can only produce an estimate, particularly as we do not know how long the war period will last. In order to prevent abuse of the privilege, there should be some annual limitation on the deduction. I suggest net income rather than gross income because the relationship between the two varies materially according to the type of business involved. Were gross income made the basis, the large-volume producers with the low net profit would benefit unduly in connection with the service company which is likely to have a large net profit out of a small volume of gross income. I suggest 15 per cent of the net as a reasonable annual limitation, and if the war period continues long enough we can later impose an over-all total fund limitation. By that time we shall have a much better idea on how much is required and how much is being accumulated for the purpose.

Investment in Government Bonds—Taxpayers who desire to take advantage of the election should be required to invest the entire fund, that is, the amount of the deduction, not merely the tax reduction, in suitable low-interest or even noninterest-bearing government bonds provided especially for the purpose. I think those who desire the protection of the creation of the reserve without the payment of taxes thereon should be willing to put the entire fund aside because it would be deducted on the theory that it will be required in the future. They should forego interest as the cost of their protection. This would provide more funds for the government and reduce to that extent the inflationary pressure resulting from increased bank deposits.

The bonds should become payable on demand within a very short time after the end of hostilities, that is to say, no more than is necessary to permit the Treasury Department to arrange the necessary financing, and at the end of that time they should bear a reasonable interest rate so as to prevent a sudden drain on the Treasury for funds not required immediately. In that manner the availability of the funds is assured and the government would not be treating as revenue that which is really a temporary borrowing.

Expenditure of the Fund—The permission to take the postwar reserve deduction should carry with it the requirement that it be expended within a given period (and I suggest three years) after the end of the war—to be explicit, I should say the end of the war production period rather than hostilities—in order to assure that it will be used for the required purpose within a reasonable period of time, and when it will do the most good.

Purposes for Which Fund May be Expended—It is my suggestion here that the taxpayer be permitted to expend the funds for any one of a number of specified postwar purposes, without being required to indicate, at the time the fund is created, the particular purpose for which it will be expended. After all, one does not know now just how reconversion will be accomplished, and even if one had definite expectations at this time, plans may have to be changed to meet changing conditions.

As to the recognized purposes, I cannot presume to state them completely and in detail. That, it seems to me, is the job for the representatives of business who are now studying postwar needs. Among others, these have been suggested and I think they are all sound:

- (1) Severance and relocation costs or wages or substitutes therefor.
- (2) Costs of reconverting, moving, or altering plant facilities for peacetime production.
- (3) Deferred maintenance (not otherwise covered by accelerated depreciation allowances).
- (4) Losses on plant asset eliminations not offset by the retention of amortized facilities.
- (5) Inventory losses, whether resulting from price declines of regular products or the disposition of war substitute or sub-standard products.
- (6) The forced entry into new or substantially new business because the former business has been eliminated by war developments.
- (7) The development of commercial or civilian business in fields that were not fully developed before all efforts had to be devoted to war production, during which period the result of prewar partial development was lost.

- (8) The use of facilities and development of business for government-owned facilities—but a voluntary expansion of operations through the operation (after acquisition) of such facilities should not be included unless by agreement the price paid therefor and resultant employment activity justify the allowance of the business development cost.
- (9) Deferred research expenses—deferred because services and facilities had to be devoted to the war effort.
- (10) Increased unemployment insurance costs due to the loss of merit ratings when war production workers are released.
- (11) Reemployment of service men.
- (12) Losses due to contract cancellations.

Recapture—Finally, I propose that if the fund is not expended for one of the specified purposes within the required time, the unexpended portion should be subject to tax recapture by the Treasury through taxing it at the rate in effect when the fund was created. Thus, if the fund proves unnecessary, the Treasury will have lost no revenue; on the other hand, the taxpayer will have had the funds available if needed. In effect, therefore, this puts the shoe on the other foot, and it is the Treasury who “waits and sees.”

It has been suggested in this connection that such a setup will lead to needless expenditures. If it should, it will do so no more than the carry-backs of unused credits or losses. To the extent that there is any difference between the effect of carrying back losses or unused credits for refund purposes or carrying back an unexpended portion of the reserve fund for taxation purposes, it will be necessary to show exactly why and for what the expenditures were made. But that is an accounting matter and I am sure that the accountants of this country can readily provide for the accumulation of the necessary data to establish what facts and figures are necessary. It is true that one cannot always go back and ascertain all the information one would like to know now, because records are maintained with the requirements of the time in mind. If we know in advance what we shall be required to establish and prove, we can develop the accounting system and the accounting data to do what is necessary. It has been suggested, for example, that capital expenditures might be classed as repairs or deferred maintenance. Perhaps there will be some who will try to get away with something like that, but those so minded are probably doing it now and are not waiting for a postwar reserve recapture possibility. It has been suggested, also, that some taxpayers may go bankrupt without having expended the fund for the required purpose, so that recapture will be im-

possible. However, if that should happen, the losses which result in the bankruptcy and inability to pay should provide carry-backs of losses and unused credits that will make recapture unnecessary. True, there may be a few here and there who will improperly divert the funds through devious means, but business as a whole should not be denied equitable treatment or placed in jeopardy merely for the purpose of preventing a few from perpetrating fraud.

I have not attempted to go into all details in outlining this plan to you; my thoughts have carried much further than those expressed here, but they have all led me to the inevitable conclusion that the idea suggested is workable and that the funds involved can be properly accounted for. Certainly our problem will be no more difficult than that which we face now under Section 722 when we have to determine, or, as the statute says, establish, what would have been earned under circumstances we know did not in fact happen; in other words, to prove what we know was not so.

CHAIRMAN MARTIN: Thank you, Mr. Cooper, for this fine address. We now have a few minutes for some of the questions which I am sure some of you wish to ask.

To start the questions, do you think there is any possibility or much hope of having such relief as you are suggesting?

MR. COOPER: About the only thing I could say is that what happened last summer was enough to get Mr. Ralph F. Paul going around talking about the carry-backs, stating why we needed them. He admitted that we ought to have something to cover postwar reconversion costs, but the law took care of it through the carry-back. I do not think that it does but if there is enough demand and discussion as we go along and we keep working on it, I think that there is a chance for further relief but business and taxpayers have to get behind it.

CHAIRMAN MARTIN: That would be one service which our group can perform for clients, to encourage the clients and ourselves to write such letters as Congressman Carlson asked us to do on this particular thing. It seems like there are two particular problems we have laid in our laps this morning, one which Mr. Cooper recited in his talk, and this one now of encouraging relief for postwar activities. The first one, of course, was the nonnecessity certificate idea, which Mr. Cooper advanced.

Are there any other questions?

MR. GEORGE DAVERIO (Firestone Tire and Rubber Company, Akron): Mr. Cooper, what makes you think the carry-backs will be eliminated?

MR. COOPER: I didn't mean to infer that they will do it. We have to go by our past experience and we know that at the time carry-forwards became most necessary, they were eliminated, because if they hadn't cut them out at that point, and I happen to be familiar with the legislative story, that there were a tremendous number of companies that would have had carry-overs and would have paid no taxes. There was no carry-back at that point. It was a matter of getting the tax. They had to take it out of the law because if they had not the

revenue would have dropped way down. Suppose it happens that in 1945 or 1946 you find a great many business corporations are not only paying no tax but they are claiming refunds of much that they have already paid. Where is our revenue to come from? And what is going to be the answer? I don't say that they are going to revise the law but if the Treasury pays the refunds, it may try to get it back in another way.

CHAIRMAN MARTIN: Are there any other questions?

MR. COOPER: I think that I should say that this is not a question of repudiation. It is a matter of tax law that can easily be changed. I would rather put it in the form of a bond. You will be more certain of getting the money.

CHAIRMAN MARTIN: I am surprised someone hasn't asked the question, "What must a company do to qualify under Section 722," maybe you all know the answer. I don't know.

If there are no further questions, we will bring this Seventh Annual Conference to a close, first, by thanking all the participants who presented papers and talks during the program, secondly, we want to thank The Ohio State University, its accounting faculty and particularly Russell Willcox for preparing such a wonderful program for us for this Seventh Annual Meeting.

I think the fact that we have had such a large attendance in spite of the fact there have been no announcements of entertainment—it is really a business program—shows the earnestness with which we all attend these meetings.

Thirdly, I would like to thank all of those who have attended, because I believe with this large attendance, which I am informed is the largest they have had in their seven meetings, should insure us an invitation back here for another meeting.

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